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MONETARY REFORM

458 In the economic history of post-war Hungary August 1946 was a turning point. The country was drifting towards complete anarchy under the impact of an inflation the speed of which during the first half of 1946 surpassed anything hitherto experienced in this field. Its effects on the currency were devastating; it overthrew the entire price structure. In some respects the heavy strain placed upon the whole economic and social fabric by the intolerable wave of inflation helped to clear away difficulties in the way of the coming monetary reform. The accelerated collapse of the monetary system reinforced the intense desire for a return to a state of normality. Thus a psychologically favourable atmosphere for a new currency was created. Nevertheless it was a dangerous gamble with anarchy.

652 From a psychological point of view it was also relevant that the gold and foreign exchange reserves of the Hungarian National Bank (representing the value of 32 million dollars), which had been removed by the retreating Germans, were traced in the United States Occupation Zone of Germany, and returned in time by the United States authorities. Skilful propaganda advertised that the new currency would be backed by gold reserves at a pre-war rate (with a minimum of 25 per cent). The new monetary unit was defined in terms of fine gold contents,[1] but convertibility into gold was, of course, neither established nor ever intended. The obligation was imposed on the National Bank to see to the stability of the currency. The denomination of the new monetary unit—forint (florin)—was chosen so as to recall the tradition of the stable florin of Habsburg days, which was still remembered by the older generation.

At the outset it was the restricted supply of the new currency that induced the public to feel confidence in it. The value of the huge amount of pengö notes was practically annihilated, as their depreciation went far ahead of the pace of their issue. The supply of money depended, therefore, on the issue of forint notes. There was an initial issue of 300 million, to give the Treasury a breathing space until the reform of taxation became operative. The amount of 300 million forint was but a fraction of monetary requirements on the basis of prices and wages, which had been fixed in advance by reference to the price structure in 1938 as a 652 starting point. Nevertheless strict deflationary credit practices 457 were maintained at the beginning, compelling trade and industry to sell off stocks and also reserves of foreign exchange. Holders of foreign exchange were encouraged to offer it to the

[1] 1 forint = 0·0757 gramme of fine gold.

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National Bank by an amnesty put in force for a limited period, relieving them from the penalty for omitting to do so prior to the monetary reform. Draconic penalties were at the same time announced for any new infringement of the exchange regulations.

The psychological and technical devices worked. It soon became evident that the farmers accepted the new money. Something like a normal interchange between the urban and agricultural sectors of the community, an interchange which had been badly shaken by the preceding monetary disorder, was re-established.

Stabilization was, of course, backed by budgetary measures. A comprehensive fiscal reform of taxation, with the aim of restoring a budgetary balance, had been prepared in advance, and was evolved on broad lines out of the pre-war taxation system. Each source of revenue was to be exploited to the utmost.

Accordingly, rates of taxation were raised considerably as compared with those in force prior to the war. This relates both to the income and property taxes and to those on consumption. Incomes exceeding 1,200 forint a year (£24 though higher in purchasing power than in England) were liable to income tax. The rate was fixed at 2 per cent in the lowest range. Incomes of 10,000 forint are taxed at a rate of 6·7 per cent. The income tax reaches maximum rates of 70 per cent for income from work and 80 per cent for income from property. These highest rates weigh upon incomes exceeding 84,000 forint. A surtax with rates ranging from 15 to 75 per cent was payable on earnings (net of tax) above 18,000 forint. An increased tax on house rent amounted to 60–80 per cent of the gross rent, leaving only 20 to 40 to cover upkeep. The purchase tax was raised from the pre-war range of 2–5 per cent to 3–10 per cent. The company tax had to be paid according to turnover, irrespectively of whether there was any net profit. The pressure placed on the taxpayer may be seen from the fact that the interest on tax arrears has been replaced by a subsidiary tax at a *monthly* rate of 10 per cent. These efforts, coupled with a severe restriction of current expenditure on goods and services, produced a marked improvement of the budgetary position. Yet the burden of reparations amounting to 1,436 million forint out of a total expenditure of 3,701 million, prevented the Government from securing a real balance. The improvement attained after the first transition period of reorganized tax administration is illustrated by the rise of the contribution of taxes and other current revenue to total receipts from only 18 per cent in August and 47 per cent in September 1946, to an average of 78 per cent for the whole

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[651] budget year. Eventually 360 million forint had to be raised by borrowing (60 million through the Postal Savings Bank in addition to the initial National Bank loan of 300 million) and 450 million from other extraordinary sources of revenue.[1]

The supply of currency, as reflected in the issue of bank-notes, is shown by the following figures:

	Million forint
31 August 1946	355·6
30 September 1946	606·6
31 January 1947	1,016·8
30 April 1947	1,258·2
31 July 1947	1,592·2

652 457 The renewed expansion of the circulation might prompt the question whether the public, with the recollection of their recent experiences, would once again begin to distrust the currency. The stabilization was strictly confined to the internal value of money. In Hungary a system of exchange control had been in force as far back as 1931. This control naturally was taken over and maintained when an economy of shortage supervened at the end of the war. Transactions arising out of foreign trade were based on official parity rates in conformity with bilateral agreements.

In spite of heavy penalties a black market for foreign exchange and gold developed with rising rates. Apart from prosecuting the participants, in so far as they could be caught, the authorities did not interfere with the black market. There was, in particular, no direct intervention to influence the rates of this market. They were regarded by the authorities as isolated phenomena, unlikely to affect the general economic situation. This view was on the whole justified, for transactions in the black market were negligible.

652 [458] However, by the autumn of 1946 an additional difficulty arose, endangering the balance between the amount of currency and the stream of goods. The poor harvest and the deficiencies of administration resulted in an acute food shortage and soaring prices. These price increases undermined confidence in the monetary reform, and black-market rates of exchange rose correspondingly. The upward movement was halted by a temporary credit restriction. A similar stiffening of the position developed in March 1947 in connexion with new difficulties in food supplies. It was checked by the same weapon of short-lived deflation. This was effected by enforcing the maximum limit of the note issue and by giving instructions to the National Bank

[1] These consisted mainly in the profit from the revaluation of the National Bank gold reserve and in the proceeds of the sale of goods obtained within the framework of UNRRA relief and the U.S.A. loan in kind.

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to apply stricter principles of selection, especially in regard to the maturity of bills discounted. Though in both cases only temporary success could be achieved, the Government managed to demonstrate that not only upward movements but also setbacks in commodity prices and in exchange rates on the black market might occur. This proved to be sufficient to stave off an inflationary disposition. The effects of the uneasy balance established were not far-reaching enough to stimulate saving and accumulation of capital in the form of money. It was not monetary developments, however, that primarily impaired private savings, but much rather the extremely low level of incomes and the lack of political confidence on the part of the limited number of persons with higher incomes. Yet the currency created by the reform of August 1946 performed its functions as a medium of exchange satisfactorily. No doubt inflationary pressure was present in 1946–7 as well as later on, more intensely in the event of poor crops and less so when food supplies were adequate.

Summing up, the monetary reform did not succeed in creating a completely stable currency. But it did end a period of fantastic inflationary excesses by establishing a financial system kept under control, and it presented the planners with an instrument which, though far from perfect, was nevertheless useful enough for their purpose. A basis for economic calculation was created, though in the case of long-term plans allowance had still to be made for changes in the price level. Last but not least, the new monetary system, though incomplete when measured by the stricter standards of economic theory, was, after the experience of the past, appreciated by the workers and the peasants. Beyond doubt the new currency contributed to the improvement of labour productivity. Thus the measures carried through in the field of finance in 1946–7 were with good reason regarded as a preparatory step for the introduction of a planned economy.

A NEW PRICE STRUCTURE—DEFICIENT CONTROLS

In view of acute shortages, the fabric of the economic control introduced during the war was maintained in post-war Hungary. Exchange regulations were coupled with a system of import quotas. The supply of raw materials, whether foreign or domestic, was allocated among users by the authorities. In 1946–7 rationing comprised all important sorts of food and certain other products like domestic fuel and soap. But, with supplies quite inadequate, food rations were fixed at levels covering

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the economic functions acquired so far by the Government, combined with the power to control credit, investment, raw-material allocations, prices, and wages, would suffice to give effect to the Plan without further measures of nationalization. There is evidence that even the leaders of the Communist Party shared this opinion for the practical reason, if not for any other, that further nationalization could not be coped with by the bureaucratic apparatus.

In post-war Hungary, naturally enough for an economy of shortage, war-time controls were maintained.[1] Beyond that, as soon as the monetary reform had been accomplished, certain steps pointing towards a planned economy were taken.

In view of the extremely low capital resources, the authorities decided to introduce a system of credit rationing. An inter-departmental committee was set up under the auspices of the Ministry of Finance to decide the allocation of credit, in co-operation with representatives of the National Bank. The task of this committee was to make the amounts of credit granted conform to the ceiling prescribed for the issue of bank-notes. The ceiling for the note circulation was from time to time fixed by the Supreme Economic Council. Lendings of the National Bank were completely, those of the commercial banks partly, subject to the decisions of the committee. These decisions were guided by the prevailing opinion, based on general economic considerations, as to the urgency of the credit. To mitigate the rigidity of the system, a certain percentage (though gradually decreasing) of the resources of the commercial banks could be lent without central control.

Another agency which was in a position to supplant the mechanism of the market was the Raw Materials Board. The Board, in virtue of its authority to decide on the allocation of fuel and raw materials, whether they were home produced or imported, exercised wide powers of tightening control. However, the manner in which the Board used its powers did not amount to systematic planning.

The idea of the introduction of planned economy first began to take shape at the end of 1946. Communists and Socialists did not confine themselves to advocating the idea. Both parties produced draft plans, making use of expert advice, with the aid of departmental staffs placed at their disposal. The Communists asked, of course, an expert from Russia for assistance, while the Social-Democrats profited by the expert knowledge of an economist of Western outlook.[2]

[1] See p. 13.

[2] The expert of the Communist Party was E. Varga, that of the Social-Democratic Party, Nicholas Káldor.

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BUDGET AND CREDIT

652 During the year of the monetary reform efforts were concentrated on achieving a balanced budget. It was a hard task in view of the heavy commitments for reparation and the burden loaded on the Treasury by the deficits of public enterprises. In spite of stern measures to cut current expenditure, requirements could be met only by the aid of extraordinary revenue, amounting to more than 20 per cent of the total. The Plan called for a reversal in the relation of tax revenue and expenditure. The financial conception was that the essential part of the means to be used for investment should be provided from surpluses of the Central and local government budgets. It was anticipated that the general rise of production induced by the Plan would [651] secure ample tax revenue. Moreover special taxes on property were introduced to support the financing of the Plan.[1]

The financial plan for 1947–8 provided for investment to the total amount of 1,796 million forint, to be met from the following sources (in million forint):

CENTRAL GOVERNMENT AND STATE ENTERPRISES

	million forint	
Surplus of ordinary revenue		489·5
State enterprises	122	
Capital levy	515	
Loan	200	
Total extraordinary receipts		837·0
		1,326·5
Local government		269·6
Joint Soviet-Hungarian companies		42·5
Co-operatives		36·0
Private investment		121·4
		1,796·0

The actual out-turn differed widely from the estimates. Investment at 2,494 million forint exceeded the amount anticipated by nearly 40 per cent. Of the extraordinary receipts, the capital levy yielded only 193 million, the State enterprises 50, and no loan was issued.

The gap to be covered was nearly 1,300 million. In view of those deficiencies and an additional requirement of almost 700 million, the Central Government's budget provided a surplus of 833 million, or 343 million above the estimate. Local govern-

[1] They included a capital levy to be paid in instalments in the course of three years. The lowest rate for property exceeding 75,000 forint (£1,500) was fixed at 6 per cent, the highest rate, burdening property of more than 2 million forint (£40,000), at 25 per cent. This tax was supplemented by a levy on the accretion of property (with 1939 as the basic year) applying rates from 25 to 75 per cent.

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ment produced 529·7 million or 260 million above; private investment contributed 275·7 million or 154 million above; trade agreements provided 73·5 million from abroad. After allowing for a small deficiency on the other two items, the amount available towards the 1,300 million was just 800 million. Substantially the deficiency was met by advances to the amount of 454 million from the National Bank.

Current tax revenue fulfilled expectations. There was a spectacular rise in conformity with expanding production, as shown in the figures of the budget accounts.

	1946–7	*1947–8*
	in million forint	
Receipts		
Current revenue	2,891	6,047
Borrowing or other extraordinary sources	812	350*
Expenditure		
Current, on goods and services†	2,265	3,758
International commitments	1,436	1,709
Investment under the Plan	—	833

* 193 million forint proceeds of the capital levy, the rest from the sale of stocks of commodities, participation in the profits of the National Bank, coinage.
† Including deficits on nationalized industries and subsidies.

Within the budget 833 million forint were provided for financing the Plan. Yet the figures given by the Planning Department show a considerably higher amount as contribution of the Central Government for the purposes of the Plan.

SOURCES OF PLAN FINANCE

	Planned	*Actual*
	in million forint	
Central Government	1,326·5	1,565·6
Local government	269·6	529·7
Joint Soviet-Hungarian companies	42·5	27·5
Co-operatives	36·0	22·0
Private investment	121·4	275·7
Advances from abroad (based on trade agreements)	—	73·5
Total:	1,796·0	2,494·0

The contribution of the Central Government includes, besides the item in the budget, the contributions of the nationalized enterprises[1] (covering also investments which had been reckoned as private enterprise, because they had made them prior to nationalization). It also includes the loans granted by the National Bank to the amount of 454 million forint.

In the year of the monetary reform, before the Plan, recourse became necessary to the National Bank, though only to a

[1] As distinct from 'State' enterprises. This latter term denoted enterprises, such as railways and postal services, which had been owned by the Government before the war and the accounts of which had been included in the budget.

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652 moderate amount to finance investment, and the Plan accentuated the existing inflationary pressure. Capital accumulation was inadequate to meet requirements within the limits of sound financial policy. In spite of all efforts to raise tax revenue, and the pressure exerted on nationalized enterprises to produce surpluses for the Treasury, about one-fifth of total requirements had to be provided for by loans inflationary in character.

This over-straining of financial resources was naturally reflected in the state of the National Bank. Its bill-portfolio (bills of private and public concerns) rose during the first nine months of the Plan—August 1947 to April 1948—from 920 million to 1,680 million forint (the movement in the following months of the first Plan year was obscured by the change-over in the banking system). By the end of the twelve-month period the note circulation had reached 2,224 million compared with 1,592 million forint in July 1947.

INVESTMENT AND PLAN CONTROL

454 With total investment exceeding the programme the distribution of investment over the various branches of economy differed widely from the scheme originally planned.

INVESTMENT 1947–8 (CURRENT VALUES IN MILLION FORINT)

	Capital Programme	*Actual*	*Percentage of increase*
Agriculture	579	688	18·7
Mining and manufacture	555	792	43·0
Communications	427	545	27·6
Buildings, social services	235	469	99·0
Total:	1,796	2,494	38·9

In considering these swollen figures it should be recalled that their increase was to a major part due to inflationary price developments. According to official sources this change in prices was responsible for an increase of about 28 per cent, leaving a margin of roughly 10 per cent for increases in volume. If this statement is correct, it follows that in terms of real value investment in agriculture was less than the estimate, while that in communications was in line with the Plan. Thus real increases were confined to investments in industry and building. Within industry it was in the first place power production and in the second engineering which exceeded limits set for them in the programme. This was in accordance with the fundamental ideas of the initiators of the Plan. On the other hand the sharp rise in building activity was a sign of deficient control. The big

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special credit facilities and priorities in using tractor stations, and were favoured in many other ways. In spite of these benefits and a relentless propaganda coupled with elaborate methods of pressure, land collectivization remained in an embryonic stage. By the end of 1949 it was claimed that about 1,500 producers' co-operatives, cultivating 370,000 yokes of land, had been established. This would amount to 2·6 per cent of the total agricultural area. Even these moderate figures may be over-statements, as possibly not all the co-operatives concerned are of the most 'advanced' type, which merges the holdings of the individual members. Moreover, this kind of co-operative was mostly established on land recently acquired by the Government under the right of pre-emption, or through confiscating *kulak* holdings, and redistributed on condition that the new owners joined the advanced form of co-operative.

So far the changes in the organization of agriculture as brought about by the land reform were slight. Yet the rural districts had been stirred up and their atmosphere poisoned. Some detrimental influence on productive activity may eventually result, but no signs of it have been discernible up to now. The reports on the achievement in agriculture neither substantiate accusations of *kulak* sabotage nor do they indicate any relaxation of assiduity in cultivation because of anxiety about the ownership of land. The terror applied in collecting the grain and other produce, which the peasants were bound to deliver in order to ensure public supply, may partly explain their zeal in growing adequate quantities.

ADOPTION OF THE SOVIET PATTERN IN BANKING

In April 1948, with any serious political opposition already excluded, it was proposed to recast the Hungarian credit organization. By that time the nationalization of the leading banks had been completed. As already stated that measure, extending as it did to the subsidiaries of the institutes concerned, subjected over 80 per cent of the credit apparatus to public control. Nationalization, as it was decided upon in 1947, was intended to avoid the disruption of existing units, and to enable them to restore former international relations. A reorganization of banking undeniably appeared necessary. It was already overdue during the inter-war period, when the solution of the problem was adjourned because of the rivalries of competing groups and the lack of determination of the financial authorities. There is little doubt that a reasonable organization could have been reconciled with the preservation of ties with Western

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652 453 financial markets. Yet the break-up that ensued was calculated to sever existing links. The new State banking system was introduced gradually as from May 1948, and the old structure disappeared.

The entire current banking business was transferred to the National Bank which took over the assets and the liabilities of the other banks. Thus the Central Bank, endowed with the right of note issue, was turned into the exclusive source of credit. It provided enterprises directly with working capital through the instrumentality of the 'single-account' system. For an enterprise placed under this system, the National Bank had the monopoly of banking services. All its financial transactions had to pass through its single account. In particular loans providing working capital were credited to it.[1] From the outset nationalized enterprises and other public concerns came under the system. Any private enterprise, applying for credit to the National Bank or to the Treasury, might be drawn in, thereby being practically placed under public control.

Thus the National Bank came to provide for the financial requirements of the publicly-owned concerns and, to a considerable extent, also of those privately owned. For the residue of credit operations certain other institutions are assigned.

(1) An Investment Bank was established to finance and control investment activities in mining, industry, transport, and in important branches of building. The Bank is practically the financial section of the Planning Department. The funds at its command are derived first of all from the central and local government budgets. The amounts earmarked in these budgets for investment are transmitted to the Bank. It has at its disposal another source to draw upon for the purpose of allocating long-term credits: the National Bank. Finally it is the Investment Bank that handles the depreciation fund of Hungarian industry. All enterprises—public and private—pay regular contributions to this fund in proportion to their sales.[2]

652 457 (2) The Bank of International Trade was endowed with the monopoly of banking transactions connected with foreign trade. One of the former big Budapest banks, which, like the other banks, had already handed over all the other parts of its business to the National Bank, was established in this special capacity. However, in one respect the monopoly of the Bank for International Trade appears to be restricted; in transactions with Soviet Russia it is required to co-operate with the Russian-owned Hungarian Bank of Commerce and Industry.

652 453 (3) The National Savings Institution first operated as a section of the National Bank. In a second phase the section was promoted to

[1] The purport of this system from the point of view of financial control will be discussed in Chapter IX.

[2] See comments on p. 86, below.

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be a separate institution, a change which did not substantially alter the former position. In it, the savings banks of the country, including the Postal Savings Bank, were merged. Besides collecting deposits through its network of branch offices, it acts as a bank for private enterprise. It grants short-term credits to small-scale industries and retail trade. But the credits granted fall short of the deposits collected, and the excess is transferred to the National Bank to support the credit operations of the latter. According to an expert statement the direct lending of the Savings Institution amounted to hardly 10 per cent of total deposits in July 1949.

(4) The Bank of Co-operative Societies, a long-established centre for co-operative credit, acts as the bank for agriculture. Though it receives deposits, this branch of its activity has so far shown poor results, and it depends, therefore, for capital resources on the National Bank.

Outside the Hungarian banking system the Russian-owned Bank already referred to enjoys a status of *de facto* extra-territoriality. It is the banker of the various Russian enterprises, headed by an agency for the management of Russian property. The Bank was originally Austrian-owned, and was taken over by the Russians in pursuance of their interpretation of the Potsdam Agreement. Other foreign banks were wound up, as no scope was left for their activities.

From any description of the banking system of Soviet Russia it is clearly seen that the Hungarian Communists faithfully fulfilled their task of copying the Russian organization. The State Bank, as the sole institution for short-term credit, and around it a few specialized agencies as distributors of the funds made available for planned investments, are the characteristics of the credit system adopted in the Soviet Union in 1930.[1] However, when building up the new system, there was a fundamental difference between what had to be done in Russia on the one hand and what in Hungary on the other. The Russian Bolsheviks had to fill a vacuum, as vast territories under their rule were without any credit organization. The Hungarian Communists had, on the contrary, first to destroy a fairly well developed credit system before introducing the new pattern.

It was a peculiar incident in the course of the Three-year Plan that the pattern of economy changed during its progress. To initiate these changes was a daring experiment, which amounted, in fact, to an alteration of the steering mechanism while under way.

The following table shows the progress of nationalization in the course of the Three-year Plan.

[1] Alexander Baykov, *The Development of the Soviet Economic System: an essay on the experience of planning in the U.S.S.R.* (Cambridge University Press, 1946).

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THE PROPORTIONS NATIONALIZED (PER CENT)

	July 1947	*July 1948*	*Dec. 1948*	*Dec. 1949*
Mining	91†	91	91	91
Manufactures	37·5	80	87	92
Transport	98	98	98	98
Banking	80	95‡	95	95
Wholesale trade*	—	16	75	100
Retail trade*	—	—	20	30
Agricultural land				
(*a*) State-owned	2	2	—	4
(*b*) Producers' co-operatives	—	—	—	2·6
Forestry	100	100	100	100

* Including publicly-owned co-operatives in terms of turn-over.
† The rest foreign-owned.
‡ The rest Russian-owned.

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CHAPTER VII

THE PLAN IN FULL SWING

SPEEDING UP INVESTMENT

DURING the first Plan year a start was made which appeared favourable for the planners' claims. They could point to a considerable rise in industrial production. In spite of a bad harvest, the standard of living of the workers improved, while at the same time investments on a large scale were carried out. In some places the picture was obscure. There was the ominous lack of effective price control, and, in the background, the disparity between incomes and the supply of consumer goods. There were shortcomings in exports, and finally there was unevenness of fulfilment in production and investment. Yet, in overall figures the programme of industrial production was fulfilled, and even slightly surpassed, if statistics involving an evaluation of a wide range of manufactured articles could be regarded as precise indicators. This seems to have been a surprise to the planners themselves, for, in reviewing the results, the responsible official of the Politbureau divulged that, owing to deficient information on production levels at the time when the Plan was prepared, output had exceeded expectations from the beginning.

It might have appeared tempting to enlarge the programme as soon as the possibility of better achievements became manifest. And soon there were more definite grounds for speeding up the execution of the Plan. One of these was a 50 per cent reduction of reparations due for the period following July 1948. This concession was made by the Soviet Government after the decisive political changes in the course of the spring of 1948, in particular the destruction of the Social-Democratic Party and the nationalization of manufacturing industry. The reduction was calculated to save budget expenditure exceeding 600 million forint a year; it was assumed that this amount could be diverted to investment. Though later on these hopes turned out to be unfounded, the prospect of saving on reparation account was used as an argument in favour of stepping up the capital programme. In fact, more than the amount of the reduction was required for the increase in defence expenditure, for the Plan, after its successful start, was more closely linked with military preparedness.

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435 465 511 granted; their effect on purchasing power appeared reinforced by the reduced cost of living. These developments, combined with an increased output of manufactured consumer goods, resulted in improved living conditions. There can be little doubt that more abundant supplies resulted in an appreciably higher standard of living in comparison with the level at the start of the Plan, though statistical data revealing the degree of improvement are lacking.

INVESTMENT AND FINANCE

652 454 The first and one of the most important implications of the decision to shorten the total period of the Plan was the speeding up of the capital programme. For the financial side of the programme, the Government disposed of a banking system shaped according to the Soviet pattern, and entirely under their command. The bulk of investment was naturally financed, as before, out of the budget. It became a characteristic feature of estimates of investment that they represented minimum programmes. For the short second Plan period the estimate had been 1,100 million forint, while actual investment worked out at 1,530 million. For 1949 the corresponding figures were 4,300 million and 5,660 million forint. In a final report the latter amount appears to be raised by a further 630 million forint. In view of the tightness of financial controls, any exceeding of the capital programme (unless consequential on authorized increases in wages or prices) was impossible without a previous screening and consent of the authorities. An extension of investment, whether initiated by some Government agency or by the executives of one of the concerns, was to be fitted into the monthly financial plan, which was drawn up by the National Planning Department in co-operation with the Ministry of Finance, and had to be approved by the Supreme Economic Council. As the speeding up of the capital programme mostly affected heavy industry the extension of which was, not solely for economic reasons, the concern of the Government, initiative evidently lay mostly with the Government. Both the Government and the Planning Department were intent on extending the capital programme to the limit of technical possibility.

The increasing financial strain is reflected in the following figures:

	Monthly Average of Investment (million forint)
Plan period I	.208
Plan period II	306
Plan Period III	470–520

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Investment was accelerated by 50 per cent in the second period compared with the first, and subsequently again by 50 or even 70 per cent in the third compared with the second.

In an endeavour to raise revenue for meeting requirements a new profit surtax was introduced, charging company profits which exceeded 5 per cent at rates of 30 to 50 per cent. Except in the very limited portion of industry which had not been nationalized the financial effect of this measure was nugatory. Simultaneously a purchase-tax reform was carried out, accompanied by an increase in rates. The reform secured that this form of taxation should remain the most important single item of revenue, with proceeds exceeding those of direct taxes. Further measures were taken thoroughly to exploit all sources of taxation, whether old or newly created. It seems that in spite of all these efforts the Treasury failed to raise revenue on the scale required by the increase of expenditure.

Provisional budget returns published in the official *Statistical Bulletin* relating to August-December 1948 show 3,697 million forint total revenue and 3,920 million forint total expenditure. Later, modified final figures were published disclosing a moderate surplus in place of the deficit of some 200 million resulting from the figures quoted above. It should be noted, however, that in an economy with industry largely nationalized, budget results are not conclusive without an analysis of National Bank loans. The nationalized enterprises being the most important borrowers from the Bank,[1] nothing seems easier than leaving deficits concealed in their accounts in order to relieve the budget, if this kind of window-dressing is wanted.

BUDGET ACCOUNTS, AUGUST-DECEMBER 1948
million forint (provisional)

Revenue	
Current items	3,541
Capital levy	118
Other extraordinary receipts	38
Total	3,697
Expenditure	
Current items	1,815
Deficits and subsidies	700
International commitments	449
Three-year Plan	955*
Total	3,919

* According to a statement based on computations of the National Planning Department: 985·1 million forint.

[1] According to a statement of the National Bank the participation of State-owned enterprises in the total of its loans reached 70 per cent by the end of 1948.

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652 Though reparation payments were appreciably reduced, the rate of total expenditure worked out at 50 per cent higher than in 1947–8. The following table reflects changes in the different groups of expenditure:

EXPENDITURE IN MILLION FORINT (MONTHLY AVERAGES)

	1947–8	*Aug.-Dec. 1948*	*Difference per cent*
Current items	249	363	+45
Payments for deficits and subsidies	64	140	+120
International commitments	142	90	−36
Three-year Plan	70	191	+170
	525	784	+50

Thus while there was a saving of 52 million on reparations, the excess of expenditure on other items, amounting altogether to 310 million forint monthly, was accounted for by the following: investment under the Plan, 121 million; payments for deficits and subsidies, 76 million; and current expenditure on goods and services, 114 million. Simultaneously with the sudden rise in the requirements for financing the Plan, there was a considerable increase in the current cost of administration. The higher outlay was partly explained by the necessity of adjusting civil servants' salaries which had lagged relatively far behind wages. The establishment of new departments and the extension of the scope of public functions also contributed to the increasing expenditure. The striking increase in the expenditure to cover deficits and subsidies needs some special explanation. There is reason to believe that these items included a growing outlay for armaments; some part of the increase in current expenditure might have been for the same purpose.

As to the sources from which the Plan was financed, 64 per cent of total requirements, slightly above the proportion recorded for 1947–8 (62 per cent), were provided by the Central Government. The indebtedness of the Investment Bank to the National Bank increased by 260 million forint. As in the case of the first Plan period, the Government, in its determination to rake out all possible sources for financing the Plan, succeeded in raising a substantial part of the funds needed by draining off purchasing power. Yet a residuum of about 17 per cent had to be secured by loans inflationary in character.

Information has been withheld in regard to the manner of raising the huge amount required for investment in the closing Plan year. According to the budget estimate for 1949, a total expenditure of 9,275 million forint was to be fully covered by tax revenue and surpluses of nationalized enterprises. For capital

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expenditure within the Plan 3,320 million forint were provided in the budget. As to the out-turn, the Minister of Finance declared in a speech delivered in December 1949 that the total expenditure was expected to approximate 13,000 million forint, an increase corresponding to that of the revenue. For investment under the Plan an amount exceeding the estimate by more than 1,000 million forint was appropriated.

The expansion of economic activity had to be supported by adequate credit facilities. During 1948 movements in the accounts of the National Bank were largely governed by technicalities in consequence of the reshaping of the banking system. The reform resulted in a concentration of the total current banking business within the National Bank. Note circulation, an item presumably unaffected by these shifts, rose between August and December by 27 per cent, a change in accordance with seasonal trends and the general expansion of the economy.

For 1949 the marked increase in production and employment was reflected in the upward movement of the loans granted by the National Bank, and in the corresponding movement of deposits, while the note circulation, quite out of accord with seasonal and general trends, declined in the second half of the year. It is true that, in connexion with the banking reform in 1948, provision was made for restricting the use of currency in settling business transactions. A ruling was then put into force according to which between nationalized enterprises amounts exceeding 500 forint should be paid by transfers on accounts. For payments outside this circle the limit for the use of currency was drawn at 3,000 forint. It is surprising, however, that this ruling should suddenly have had such a palpable effect as from the third quarter of 1949. Irrelevant though it is whether a strain on the financial system manifests itself in an increased circulation of bank money or of currency, it is not quite indifferent, in a psychological sense. It was on the note circulation that the attention of the Hungarian public, unversed in monetary questions, was focused. The following table shows the movements pointed out:

NATIONAL BANK OF HUNGARY

	Gold	*Foreign Exchange*	*Bills*	*Loans*	*Notes*	*Deposits*
			in million forint			
1948						
July	403	50	730	778	2,224	730
December	412	153	50	5,982	2,816	3,691
1949						
June	412	207	3	7,147	3,007	4,620
September	445	115	3	8,112	3,175	5,335
December	480	32	—	8,537	2,629	6,492

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COMPARISON OF NOTE CIRCULATION

in million forint

	1947	*1948*	*1949*
June	1,468	2,070	3,007
September	1,834	2,506	3,175
October	1,868	2,585	3,052
November	1,829	2,543	—
December	1,992	2,816	2,629

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Conspicuous changes were brought about by the Three-year Plan in the Hungarian economy. In the first phase the unfolding of the Plan was gradual. An ambitious capital programme was carried out to lay the foundations for later expansion. Employment in industry was increasing slowly, while a struggle against disabling food conditions was going on. Shortage of food played havoc with price control and wage policy.

During the second phase the capital programme was pushed forward at an accelerated pace. In industrial production the rate of increase, though considerable, was slower than at the initial stage. Expansion of productive activity was such that industrial unemployment was eliminated, and part of the unutilized man-power in agriculture was absorbed. The building trade, which had been very depressed up to the end of 1948, was included in the expansion. Its revived activities were in part directed to supporting the rearmament programme, and in part anticipated the requirements of the Five-year Plan to be started in January 1950.

Owing to more favourable crops, food conditions became normal and price control more efficient. But productivity in industry did not improve to the extent hoped for. In spite of all efforts to produce results by Stachanovite devices, the problem of reducing costs in manufacturing industry was not mastered.

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185 cerned. One reservation, however, appears to be justified. The stress placed on the development of heavy industry presumably hampered the expansion of light industry on such a scale as would have been attainable without the compulsion exerted by the Plan.

THE RATE OF CAPITAL ACCUMULATION

454 652 There is a peculiar dynamic quality inherent in the economic plans in Eastern Europe. All of them are intent on imposing a pace of development which implies strenuous present efforts for future results. An increased capital equipment has to be created to attain increased productivity. As foreign capital aid was excluded, additional equipment had to be produced from domestic resources, and to this end all available reserves had to be mobilized. It was this spirit of austerity, calling for individual sacrifice, which underlay the decision to devote 10 per cent or more of the national income to a capital programme, notwithstanding prevalent shortages.[1] This decision doubled the rate of net investment compared with pre-war, while a considerably reduced national income was also burdened with reparations to the amount of 6 per cent.

The grim determination of the planners to speed up reconstruction and the development of productive power placed the responsibility for the adoption of measures to secure an adequate capital supply on the central authorities. Individuals could not conceivably be allowed to decide upon the rate of accumulation according to their own preferences for future as compared with present goods. Compulsory saving became imperative, and it was effected mainly through taxation. From the outset all possible sources of revenue were strained to the utmost in order to produce a surplus large enough to finance the capital programme. The special capital levy proved a failure. It provided approximately 200 million in the first Plan year towards total requirements amounting to 2,500 million forint. The principal part of the funds needed was, in fact, raised from the general revenue. Consequent on the necessity to secure the means [651] wherever they were available, an intricate multiple system of taxation was maintained. Though direct taxes with progressive rates contributed a considerable part of the revenue, the mainstay of Government finance was the purchase tax, together with other duties and monopolies falling on consumption.

A system of compulsory savings through taxation does not exclude other devices for promoting savings. Spending can be

[1] This relates to the first Plan year. In 1949 net investment climbed up to 18 per cent.

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restricted by controls and rationing. But controls must be strict, and the average income level must be high enough to leave a margin after covering the rationed products. These conditions were not present in Hungary. The Government were the more intent on encouraging voluntary thrift, in the hope of closing the gap between the amount of investment and the surpluses available for capital expenditure in the central and local government budgets. To this end high rates for savings deposits (3 to 9 per cent according to maturity) were fixed. The results achieved were poor. Even conceding the attractiveness of high interest rates, conditions—economic and political—were all against a favourable result. In April 1948, before the re-casting of the banking system, deposits totalled 1,440 million forint. Considerable as the rise was compared with the early post-stabilization period, the amount attained worked out at no more than 15 or 16 per cent of the total deposits in 1938 in terms of real value. But even in the inter-war period with bank credit on a normal scale, no proper capital market to finance investment operated.

INTEREST RATES AND THE DIRECTION OF INVESTMENT

In a system in which investment and savings are determined by the decisions of a central authority, no functional connexion exists between interest rates and the volume of investment. It rests with the central authority to fix interest rates arbitrarily, or to renounce the use of interest altogether. The Hungarian planners decided that the Investment Bank should allot long-term capital to public enterprises free of interest, except that a token rate of 1 per cent could be charged, apparently to cover the costs of running the bank. For co-operatives and applicants that are partly publicly owned, the rate of interest on capital borrowed from the Investment Bank amounts to 3 to 5 per cent. Other debtors, i.e. private enterprise, are charged with 7 to 10 per cent. By far the greatest part of the investments financed from the budget through the instrumentality of the Investment Bank comes under the first head, and does not bear interest.

In contrast with this practice, interest is charged on short-term credit to finance working capital, for public as well as for private enterprise. According to arrangements put in force under the Plan the interest rate amounted to 5 per cent for nationalized enterprises, to 12 per cent for other industrial enterprises, and to 18 per cent for commercial firms. It may be mentioned that prior to the war a rate of 12 per cent was not unusual for normal bank credit (inclusive of the margin earned

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652 453 by the private banks). When the private banks disappeared, the differential rates were directly charged by the National Bank.

The following special interest rates were in force for agriculture:

	per cent
(1) For co-operatives running collective farms	5
(2) For other co-operatives and for members of co-operatives in category (1)	9
(3) For members of co-operatives in category (2)	11
(4) For other debtors	18

The scale of interest rates can hardly be said to have been inspired by purely economic considerations. It was rather on political grounds that private enterprise had to bear considerably higher rates than that which had been nationalized. In agriculture the Government were intent on favouring collective farming by discriminative credit practices. 'Working' peasants were allowed to obtain credit on conditions similar to those prevailing before the war. For others (excluded from the co-operatives) a prohibitive rate of 18 per cent was fixed, though it was hardly more than nominal since those owning holdings over [661] 25 yokes were denied credit facilities. One decisive consideration was, apparently, to exploit even rates of interest as a weapon of class warfare.

652 454 In a capitalist system based on free competition, the investment market determines the allocation of resources among the various openings for capital enterprise, and the long-term rate of interest is its principal instrument for the purpose. The Hungarian Plan rejected that mechanism, and the question remains by what considerations the Government or the Planning Department was guided in deciding upon the allocation of capital resources among industries. At the inception of the Plan there was hardly any alternative to deciding arbitrarily upon the direction of investment into the various channels in conformity with preconceived ideas about the relative importance of capital-goods industries and of some outstanding consumer-goods industries. But as, in the course of economic progress, the application of the Plan became more and more intricate, this first rough approach had to be superseded by more discriminating methods. Under conditions when production provides only for bare necessities a programme based on nothing better than guesswork will contribute to meeting consumers' needs. As soon as the economy progresses beyond this low standard, divergencies between the anticipations of the planners' and consumers' wants are likely to arise.

652 475 The exemption of publicly-owned enterprises from being charged with interest on their investment would not itself pre-

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clude an internal calculation of interest for the use of the planning authorities for the purpose of cost accounting. The inclusion of a hypothetical charge for interest would make more realistic the obligation imposed on the enterprises to earn profits for the Treasury. Net surpluses so calculated, after taking due account of costs, including the cost of capital engaged in the enterprises, might serve as a criterion for the guidance of the planners in comparing the desirability of investment. Yet the 'profits' delivered to the Treasury are not the outcome of an appropriate system of accounting. They are derived from the excess of receipts from sales over total expenditure. Replacements are provided for from a centrally-managed depreciation fund into which the concerns are bound to pay contributions separately fixed for each branch of industry. Characteristically enough these contributions are also based on the sales of the enterprises.[1]

The absence of a calculation of capital costs from the account makes the prices of the products of heavy industry relatively low. The resulting distortion of the price structure might have been corrected by varying the percentage to be added to the costs (consisting of expenses for materials, wages, replacement, and maintenance), on account of the margin of profit to be delivered to the Treasury. But that was not done; the margin was equal for the whole range of industry.

Perhaps the underlying idea was that the paramount purpose of fostering the expansion of heavy industry would be furthered by fixing low prices for its products. But it would seem that the low prices were of little practical effect in stimulating demand. Where, as in most instances, the products were bought by one publicly-owned enterprise from another, the price was merely a matter of book-keeping, and losses on the one side balanced gains on the other.

On the other hand, in the case of exports, any underpricing inflicts a definite loss on the economy. This point is not unimportant in view of the considerable deliveries of the products concerned to the Soviet Union.

The objection might be raised that a more realistic method of cost accounting would be of little relevance for directing investment when the greatest part of it (i.e. that in heavy industry) was determined regardless of economic considerations. Yet, whatever the objectives adopted on political grounds might be, it was possible to approach them in ways either more or less in accord with economic principles. The Planning Department certainly drew up calculations to enable a rough comparison to

[1] See below, p. 86.

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454 652 be made between capital expenditure and anticipated economies, taking account of the time factor when schemes of national importance were in question. To be more specific, when they had to choose between different big power development schemes, they attempted to compare the periods within which the economies to be achieved by the several schemes would equal the capital outlay to be incurred. However, this method fails to work in hundreds of ordinary cases, whether in heavy or in light [434] industry. Without the link between the consumers' demand and capital allocation, established by the use of a rate of interest in the cost calculation, it was not possible to determine accurately whether at a given moment the allocation of means to a textile-mill or a shoe-factory was more urgent. The planners did not regard refinements of this kind as matters of consequence. They believed that their targets for the production of consumer goods accorded largely with the needs of the ordinary man, and they did not appeal to the test of cost and price to determine whether at a given moment more textiles or more leather goods would have been indicated by the consumers' preferences.

454 475 652 In an economy lacking proper methods for the calculation of capital costs a danger of capital consumption arises, especially when the executives are pressed hard to remit the greatest possible surpluses to the Treasury whether genuinely realized or not. This danger was the more acute as allowances for replacement might be fixed much too low by the Planning Department. Undue cutting down of maintenance cost was another possible device for producing unreal profits. Even the men in control could only gradually discover whether this was actually taking place. On the model of Russian practice, the disregard of capital equipment as a cost factor appears to have been a point of principle. Whatever the real reason was, it is a fact that in the course of the Three-year Plan the system of accounting applied by the nationalized enterprises did not offer a reliable basis for deciding between alternative projects of investment. The practical relevance of this deficiency should not be overestimated. Calculations anticipating future developments are usually influenced by too many factors to leave a single item a decisive role. Moreover, in a planned economy the need for keeping down capital costs might often be deliberately overruled by other considerations. Even so the disclosure by current methods of accounting of what is being done would be useful. The Hungarian authorities deprived themselves of a convenient pointer, even though subsidiary in importance, for indicating whether capital supply in certain industrial sectors should be extended or curbed.

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PRINCIPLES OF PRICE POLICY

The Hungarian planners' conception of price policy was to secure conditions conducive to planning. This called for a stable price level, an aim which had been pursued (though not realized) in the interval between the monetary reform and the initiation of the Plan. Thus the guiding idea for price policy at first adopted under the Plan was to use the existing controls to establish and maintain a stable price level as an adequate basis for calculation. But presently the objective was modified in that a gradual reduction of prices at a later stage was aimed at. This reduction, which was to be brought about by levelling down industrial costs, was regarded as a means of raising real wages. Hopes were attached in particular to improvement in the productivity of labour, but the course of events brought them to nothing. The policy was to avoid disturbances of the execution of the Plan being caused by price movements, which would vitiate cost calculations and wage policy. Yet price policy was not regarded as an instrument of planning in the sense of bringing about adjustments of demand and production in a general way in order to facilitate the fulfilment of the Plan.

In an entirely collectivist society it would be a matter of expediency whether public expenditure should be met by taxation or by charging prices high enough to leave a margin for the Treasury to cover the cost of public services and investment under the Plan. This simple formula did not apply, however, to Hungary under the Three-year Plan, so long as some parts of manufacturing industry, handicrafts, retail trade, and, above all, agriculture were in private ownership. The co-existence of public and private enterprise called for a system of taxation to be applied to the whole of the economy. Soon after the general nationalization of manufacturing industry the authorities declared that the nationalized enterprises should pay taxes to the same extent as under private ownership. It followed that taxes had to be included in the calculations of Government-owned concerns. In addition these concerns had to deliver surpluses to the Treasury. In the budget for 1949 former sources of revenue were topped by a new one, the profits of nationalized enterprises. The margin between the prices charged for the public and the cost of products (without allowing for expenses centrally incurred) was to flow under two principal headings into the Treasury: taxes on the one hand, 'profits' or surpluses on the other.

Under conditions prevailing in Hungary two essential points had to be considered when fixing the prices for products of

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435 Government enterprises. One of these was the relation of prices to wages. The raising of the workers' standard of living having been proclaimed as the main objective of the Plan, the price of necessities was to be kept within the means of the wage-earners. This requirement had to be reconciled with that of avoiding the danger of inflation which would necessarily have threatened if the nationalization of enterprises had involved a gap in the public revenue. Prices were therefore fixed at a level conforming with the principle proclaimed by the Treasury. Once established, this level had a tendency to become rigid. As soon as fiscal claims appeared to be satisfied, social considerations gained overriding importance. This prevented the application of sliding purchase-tax rates as an instrument of adjusting supply and demand. In some cases a dual price system was introduced for manufactured goods used by the general public. In an attempt to reconcile conflicting economic and social aspects price increases for utility types, subject to rationing, were avoided, while the prices of goods outside the utility range were sharply raised. This expedient failed, as a rule, to achieve its object, the quantity available for sales on the free market being usually a fraction too small for bringing about perceptible adjustments.

The second fundamental point to be considered when fixing the selling prices of the products of public concerns was the relation of the latter to agricultural prices. A rate of exchange between the products of the industrial and agricultural portions of the economy must be found which keeps husbandry going and, beyond that, enables the farmers to develop their equipment. This aspect of price policy was particularly important if it was intended not only, as would be natural in the case of Hungary, to rely on domestic food supplies but also to build upon agriculture as one of the main export industries.

From the point of view of the methods of price policy three groups of commodities can be distinguished:

(1) Commodities with prices kept stable during relatively long periods, if need be by granting subsidies;
(2) Commodities with prices fairly adjusted to the market situation;
(3) Commodities with prices governed by controlled cost.

Group (1) includes important foods like bread, flour, fats, and milk, also coal and basic industrial materials such as pig iron and steel, the prices of which entered into the whole industrial price structure.

435 652 In the financial year 1947–8 (August to July) the stabilized price of bread and other food required subsidies amounting to

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88·5 million forint. It was much more expensive to keep coal and iron prices at the chosen level. In fact, the combined deficit of coal mining and heavy industry, which the Government had to cover, was nearing 400 million forint. It is true that this amount included expenditure for replacements and even for disguised capital extensions. Yet another 27 million was spent on iron price subsidies, and still a share in the financing of the deficit of the coal and iron industries was passed over to the National Bank. In the next financial year the visible burden imposed on the budget became less. Price adjustments and also cost reductions may have brought some relief.

The second group of commodities, with prices adjusted on the whole to the market position, consists mainly of those food products the supplies of which are subject to seasonal fluctuations, such as eggs, potatoes, and other vegetables. For these commodities the authorities were disinclined to adhere rigidly to the officially proclaimed standard prices.[1] There was in particular a group of Moscow-trained men in key positions who had a marked preference for a freer play of the mechanism of the market. They did not conceal their contempt for market control and rationing, as being unpopular relics of war economy, and they were quick to release these controls as soon as the supply position became somewhat more hopeful. Sometimes they succeeded in their action, so that the prices of the free market established themselves between the former black-market prices and the former official ones. But in some cases in which the adherents of the market mechanism had hoped to rake out hidden reserves by the liberation of prices, the action proved to be a failure. In the absence of appreciable reserve stocks, prices soared even above the former black-market level. The price movements of the articles concerned were therefore erratic, and hardly consistent with a planned economy. As consumers were compelled, in view of the extremely low rations, to buy part even of the rationed food on the black market, a considerable part of supplies changed hands at free or black-market prices. This is true in particular of the first Plan year. Thus food prices were determined to a large extent by the actual purchasing power of the consumers, and only in part by regulations issued by the authorities.

It would hardly be correct to qualify these short-term movements, representing adjustments to momentary supply

[1] The announcement of standard prices was mostly related to local markets. Violation of these prices did not involve an offence against the Act of Price Regulation. However, in case of heavy fluctuations administrative action was sometimes taken against excessive profiteering. An essential point in fixing a standard price was that the communal enterprises for food supply were bound to keep to it.

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enterprises. Regulations applying particularly to the calculation of the profits of private enterprises require separate mention. A profit rate of either 5 or 8 per cent on sales reckoned at factor cost[1] was fixed. It depended on the ratio between the yearly amount of sales and the capital of the enterprise which of the two rates should be employed. The higher rate was applicable when yearly sales did not amount to more than double the capital; in other cases 5 per cent was admitted. It was the competent Industrial Directorate that decided upon the classification of the individual enterprises from the point of view of profit-rate calculation. How this rough and ready system works has not been disclosed.

The same base was used for determining the scale of contributions of public enterprises to the Treasury. It was the sales again that furnished the basis for the payments of the enterprises to the central depreciation fund. An earlier decree fixed to that effect a wide range of rates up to 13 per cent to be paid in as depreciation allowance. These rates were, in fact, not applied. A skeleton decree authorized the Planning Department to determine the rates. There is evidence that they were fixed at a very low level, and, though contributions according to industries varied, they were not correctly adjusted to true depreciation needs. Payments due on account of the company's tax also conformed to the sales pending final adjustment. It was, in fact, a peculiarity inherent in the whole accounting system, to rule out the capital account from calculation, a practice involving, in view of the low depreciation allowances, the danger of capital consumption.

The obligation to provide for replacements by monthly payments into a fund administered by the Investment Bank was imposed on public and private enterprises alike. The common fund of the public enterprises was subdivided into an investment section and a replacement section. The former—25 per cent of the whole—might be used, on instructions from the National Planning Department, to cover minor investments. The reserves built up by nationalized enterprises could be redistributed irrespectively of the amounts paid in by individual concerns. By this provision a central depreciation fund for industry under the command of the Planning Department was created.

Regulations on costing aimed at preventing waste and uneconomical methods of production, and a series of measures

[1] Though not essential to the working of the Plan it may be mentioned as characteristic of the position of private enterprise that only the accessory bank charges connected with loans were admitted as costs. Interest could not be included in the costs; it had to be deducted from profits. This measure evidently aimed at deterring private firms from borrowing.

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their realization appeared feasible. Priority was given to the development of electric-power production (based on deposits of lignite), as this was considered the most restrictive bottleneck in industry.

The individual quotas, covering half a year and divided up by months, became operative in so far as estimates of raw material supply were correct. These latter were a specially vulnerable point of the production forecast. In the intial stages checking of individual estimates were, except for a few key industries, incomplete. Co-operation between the planning authorities and the Raw Materials Board was loose; a deficiency caused partly by political and departmental rivalries, the Planning Department having been Communist, the Raw Materials Board, as a section of the Ministry of Industry, under Social-Democratic control during the first phase of the Plan. To eliminate this impediment, the Raw Materials Board was later merged with the National Planning Department which, at the same time, took charge of price control.

The establishment of the Investment Bank in September 1948 was another step to complete the organization of the central planning authority. The Bank was operated as the financial section of the Planning Department.

The Planning Board, established in accordance with the fundamental Act on the Three-year Plan, worked as an inter-departmental co-ordinating body. The major part of the members of this Board acted as liaison officers between the Ministries concerned with economic affairs and the National Planning Department. Regular meetings of the Board kept the Government Departments currently informed of the designs of the central planning authority, thus enabling the Departments to influence decisions at a preparatory stage.

The Planning Department played an important role in shaping credit policy. It drew heavily on the resources of the budget and was a most important claimant of National Bank credit, as a further source for financing the capital programme. Moreover, the Planning Department was closely concerned with the allotment of credit to provide the different industries with working capital, since the execution of the Plan was dependent on it. The Department participated through its representative at the Inter-departmental Committee for Credit Allocation in preparing the monthly financial and credit plans, and was also represented in the Supreme Economic Council, which gave the financial plan its ultimate shape.

It was only in June 1949, during the closing period of the Three-year Plan, that the organization at the top was altered

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647 with a view to a smoother co-operation. The Supreme Economic Council was then superseded by a People's Economic Council, with the National Planning Department, the Central Statistical Office, the Central Control Office[1] and the Office for Man-Power Economy under its direct control. The President of the Council is the member of the Cabinet responsible for economic planning. He is a super-Minister, for under his command are the Ministries for Finance, Agriculture and Food, Heavy Industry, Light Industry, Public Works, Home Trade, and Foreign Trade, i.e. all Government Departments concerned with economic affairs. As previously, the chief executive for planning was the President of the Planning Department, a member of the People's Economic Council with Cabinet rank.

ADMINISTRATION OF CREDIT

652 452 [647] A national credit plan was to be drawn up monthly, based on the financial plans of the enterprises, which had to be submitted in support of credit applications. The individual proposals were first screened by a preparatory committee consisting of the Ministry of Finance, the Planning Department, and the National Bank. The draft plan prepared was then discussed and possibly modified in the Inter-departmental Committee for Credit Allocation (p. 36), and brought subsequently before the Supreme Economic Council for final decision. There the credit plan was considered in connexion with the monthly budget estimate. The amount of money issued during the month was decided on with reference to the balance of the budget, the excess of credits to be granted over repayments, and the estimated increase of deposits (taking into account the sales and deliveries of foreign exchange as a minor factor). The Supreme Economic Council, anxious to avert inflation, fixed a ceiling for the issue of bank notes from month to month. It was understood, in principle, that a gradual expansion in accordance with the growth of production should be permitted. But the Plan dictated a quicker pace. The members of the Council, when confronted with the problem of reconciling conflicting economic and financial considerations, had to choose between reducing budget expenditure and curtailing credits. Among considerable items of budget expenditure investment was the most elastic. At times the Planning Department made concessions by postponing one or another of the projected works or parts of them. But the Council generally refrained from resisting the expan-

[1] An organization created on the Soviet pattern with the task of supervising the finances of public administration and of public enterprises.

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sionist tendency of the Planning Department. It preferred to fix the limit of the note issue below what the Plan might be expected to require, without making a corresponding cut in the budget expenditure for the capital programme. Consequently credit had to be restricted to avoid exceeding the limit. When extreme pressure was felt later in the month, the Council might revise the limit. But even so credit did have to be restricted.

The following summary of monthly credit plans shows typical seasonal changes in requirements. They are based on details thrashed out in successive committee stages.

	1948	
	August	*December*
	in million forint	
Agricultural loans	66·7	43·9
Advances to agencies for food supply	179·6	1·9
Loans to rural co-operative shops	36·6	3·0
Industrial credits	118·2	73·0
Credits for financing foreign trade	65·0	65·0
Loans for Plan investment	30·0	30·0
Others	10·0	10·0
Total:	506·1	226·8

Before applications for credit were approved by the Credit Committee, the uses to which the amounts to be raised would be put were scrutinized, and their conformity with Plan objectives was, of course, checked. Control, however, was not restricted to this prior checking of the credit applications. Accountants of the Credit Committee could at any time make inquiries as to the correct use of the amount borrowed. Departure from the prescribed line constituted a serious case of sabotage. The inclusion of a representative of the Raw Materials Board in the Credit Committee provided a link between the availability of raw materials and the allotment of credits.

Though every loan granted had to be within the Plan, applicants had no guarantee that they would obtain the amounts needed for the fulfilment of their obligations under the Plan. The ceiling for note circulation, determined by the Supreme Economic Council, necessitated a selection even among credits which were needed to carry out Plan objectives. But a postponement of the granting of a loan was not accepted as an excuse for slowing down production. The enterprise concerned was expected to find ways and means of expanding its production in conformity with the Plan. In some cases a way out was found by forced sales which depleted stocks. This expedient worked, however, only during the first phase of the Plan, when a wholesale trade with a capital of its own was still in existence. The

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sales were arranged with the knowledge and, in some instances, with the support of the public authorities, though the initiative, as a rule, came from the industry concerned. The expedient most frequently applied, however, was the postponement of less urgent commitments. The criterion of urgency was whether a postponement of payment would or would not stop production. Tax payments were suspended, as were disbursements to suppliers of raw materials, who were not in a position to threaten to interrupt deliveries immediately needed. These practices indicate the intensity of pressure brought to bear on production. Postponement of meeting obligations, while helping individual concerns to overcome momentary embarrassment, was bound to affect the financial system at other points. Tax revenue would fall into arrears, or repayments of advances by some of the suppliers concerned would be postponed. To a certain extent the method of fixing a ceiling for the note issue may have retarded monetary expansion, but it could not stop it.

Inside the credit administration there was a fundamental change in the position of the National Bank. The shaping of credit policy in the Committee for Credit Allocation rested with the representatives of the Supreme Economic Council's Secretariat, the Ministry of Finance, and the Planning Department. The members of the different Government Departments (Industry, Agriculture, Public Works) represented sectional interests. The National Bank with its delegate in the Committee provided at the same time the Secretariat of the latter. This secured the Bank an important position within the Committee though chiefly in a technical sense. For amounts not exceeding 10,000 forint (£200) the Committee delegated to the Bank its power of deciding upon the allocation of credit. The Committee itself was authorized to decide on individual loans up to 1 million forint. Above this limit decisions were reserved to the Supreme Economic Council.

The National Bank was not obliged to grant loans approved by the Committee. The Bank was expected to act with the circumspection of an ordinary banker in examining the solvency of the debtor and other circumstances which might influence the security of the credit. On such grounds the Bank had discretion to refuse credits which had been approved. The practical importance of this remnant of a credit policy of its own declined, however, with the spread of public concerns with Government-guaranteed liabilities.

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CHAPTER X

AN UNBALANCED ECONOMY

SAVINGS AND CONSUMPTION

ONE of the main objectives of the Three-year Plan was to channel a much larger part of the national income than ever before in Hungary into investment. The task was the more formidable as at the start production and national income were considerably below pre-war level. Moreover, this smaller income was mortgaged by reparations due to Russia, Yugoslavia, and Czechoslovakia. In the first Plan year 6·5 per cent was diverted on this account; afterwards reduction of the amount due and an increase in the national income reduced the burden to 3 or 4 per cent.

The total amount to be invested was determined at the outset, yet in the course of the Plan period this amount was continuously enlarged. The size of investment was the given quantity, and the means for financing were to be secured in any event. A slowing down of the Plan for lack of funds was out of the question. None the less, monetary stability having been regarded as a condition favourable for carrying out the Plan, the intention was to apply methods of financing calculated to drain off purchasing power. To this end serious efforts were made to raise the greatest part of the savings wanted through the compulsory power of taxation. Voluntary savings were expected to contribute a moderate quota (10 to 15 per cent) for financing the Plan.

Compulsory savings were effected by producing a budget surplus by means of taxation and through profits on public enterprises. Beside public savings, private corporate savings were of some importance during the first phase of the Plan. The significance of the latter faded and that of public savings correspondingly increased after the general nationalization of large-scale and medium-sized manufactures. On the strength of the ruling regarding private enterprises with approved specific plans, accumulations of these concerns were placed under the control of the Planning Department. Thus from the point of view of planning three categories of savings could be distinguished: (1) public savings, (2) private (corporate) savings under public control, and (3) private savings outside the planned sector. It is remarkable enough that categories (1) and (2)

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454 652 provided for 80 to 85 per cent of the requirements for capital expenditure during the first Plan year and the second shortened Plan period.

Private savings were to a certain extent absorbed by investments carried out outside the Plan. They were not of negligible importance in agriculture. There was an increase in livestock of an approximate value of 500 million forint (at current prices) in 1947–8. This sole item amounted to almost 20 per cent of the total capital programme of the Plan. The farmers were anxious to replace their livestock, and had at the beginning, in particular, very limited possibilities of procuring machinery and instruments. A smaller proportion of rural savings went into buildings. The thrift of the peasants, practised even under unsatisfactory living conditions, provided means for these investments. Many of them were also able to take advantage of prices on the black market. Later, in the spring of 1948, the peasants profited by the lifting of price control from a number of their products. Subsequently they were benefited by larger crops.

Within the system of mixed economy, accumulation in trade and in small-scale industry was also significant. These classes were able to take advantage of the black market. But the beneficiaries of profiteering mostly did not seek productive investments. Their earnings, derived from charging prices quite out of relation with the general income level, caused actual dissaving by many of the urban population. The possible degree [435] of profiteering may be gauged by the wide range of differences between officially fixed and black-market prices as registered in May 1948 in Budapest.

	Official Price	*Black-market Price*
	in forint per kg. (2·20 lb.)	
Bread	0·92	5·0
Flour	1·40	8·50
Fat	12·0	23·50
Beef	8·40	12·0
Sugar	7·20	12·50

Speculative profits were bound to encourage luxury production, and thus to divert resources from utilization in accordance with the Plan. When spent, the profits were likely to pass through the black market again. Gradually these illegal profits lost their significance owing to the tightening of controls, and even more, to the improvement of supplies. But evasion of exchange control and the concealment of illicit profits were among the factors which caused the authorities to abandon the idea of launching a loan in the first year of the Plan.

Failing the issue of loans, financial requirements could not be fully met by savings (whether compulsory or voluntary). During the first and the second Plan periods 15 to 18 per cent

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of the capital programme had to be financed by the National Bank. During the first Plan period the effect of these inflationary credits was accentuated by developments on the market of consumer goods, attributable on the one hand to the fatal shortage of food and on the other to the absence of planning in wage policy.

The conception which the planners accepted from the existing controls was to adjust wages and consumer incomes in general to the available amount of consumer goods. This was but a vague idea.[1] No current control was provided for ensuring a parallel movement between incomes and the flow of consumer goods. Soon prices as well as wages were beyond control. Price fluctuations on the food market made inroads on purchasing power, causing changes in the relative real incomes of the different social groups. The wage-earners did not fare badly so far as the distribution of available consumer goods was concerned. But the race between wages and food prices gave rise to an inflationary spiral. To what extent the purchasing power of the different groups of society—at times even that of the wage-earners—must have been heavily impaired by the rise in the cost of food was indicated by the fact that the official index temporarily exceeded by almost 40 per cent the level of July 1947. It was, therefore, inflation rather than controls which kept down consumption, helping the Government in directing resources towards capital-goods production. Similar developments might have been experienced in the wake of inflation in any economy without planning. A certain proportion of the funds invested was squeezed out of the consumers through soaring prices.

BALANCE OF TRADE

The heavy strain under which the economy laboured during the first Plan year was bound to affect the balance of trade. In the absence of a surplus of agricultural products, exports lagged far behind the planned level while imports caught up.

FOREIGN TRADE*

	1946–7	1947–8 actual	1947–8 planned
	at current prices		at January 1947 prices
	in million forint		
Imports	944	1,901	2,117
Exports	837	1,422	2,100
Balance	−107	−479	−17

* Referring to exports-imports on a commercial basis. Exports on account of reparations in 1947–8 amounted to 1,376 million forint, standing against an import surplus of 479 million in the balance of trade proper.

[1] Compare pp. 50–1.

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439 The configuration of the balance of trade of 1947–8 is typical of a country with expanding investment, rising consumption, and a concomitant inflationary pressure. As a result of the inflated current prices, foreign trade fell short of the amount planned by more than the comparison of figures discloses. According to the officially-computed indices of export and import prices, values in 1947–8 are to be reduced by at least 20 per cent to allow for the price increases which followed January 1947.

Returns of foreign trade ceased after 1948. In the calendar year 1948 exports and imports were nearly balanced (1,933 million against 1,975 million forint), thanks to the improved harvest of 1948 which permitted forced agricultural exports in the autumn months.

Allusions to a relative increase of foreign trade in 1949 suggest that commercial exports and imports moved around 3,000 million forint each, thus establishing a balance. It was, if really attained, a very remarkable achievement in view of the rapid industrial expansion and the resulting increased needs for raw materials and equipment. It has to be remembered that heavy reparation deliveries were still going on. A considerable export surplus had, in fact, to be produced in order to attain a balance of commercial trade.

ATTEMPT AT RESTORING INTERNAL BALANCE IN 1949

433 In contrast with developments in 1947–8, there was a fundamental change in conditions in 1949. Food shortage was eliminated and the cost of living stabilized. Wage increases in the first half of this year had different economic effects from those afforded during 1947–8. The latter were largely designed to cover minimum requirements for food, whereas a rise in wages in 1949 meant additional demand for food or manufactured goods, which apparently could be met by improved supplies. This increase in supplies was sufficient, as it seems, to offer an increased attraction for tens of thousands of work-people drawn from under-employed rural districts into industrial occupations. To some extent the supply of consumer goods exceeded current production through increasing sales of furniture and other belongings by members of the middle and professional classes who had been deprived of regular income.

452 The turn of the tide on the commodity markets now counteracted the possible effects of an inflationary injection of money. The Bank of Issue was still financing a part of the capital pro-

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gramme. In view of the vastly increased financial requirements, it is hard to believe that they could have been fully met without inflationary financial methods.[1] In 1949 the capital programme absorbed almost one-fifth of the national income, compared with one-tenth in the first Plan year. The decision of the authorities to launch a loan in autumn 1949 in support of the Five-year Plan was presumably taken in order to forestall inflationary pressure. This loan generally affected wages and salaries, and was to be paid in monthly instalments, thus tapping personal incomes. The issue of the loan was decided upon as soon as real earnings appreciably exceeded the minimum level of the early Plan period.

More effective control was enforced on the food markets, and the race between food prices and wages was stopped. A modified wage policy, combined with increased supplies of consumer goods, brought about a closer approach to a balance between incomes and supplies than had been possible in the confused conditions of the first year of the Plan. Yet the balance, even if attained, was bound to be precarious. The economy laboured under an immense strain during the closing year of the Plan. The capital programme required 18·5 per cent of the national income. And there were quite a number of further items which reduced the amount of goods available for consumption. Accumulation to some extent was going on outside the Plan. The resources for increased private investment in agriculture were provided by more satisfactory harvests and by the expansion of livestock. An item of minor importance, which was still continuing, was investment in small-scale industry. Reparations were due, though imposing a relatively diminishing burden on an increasing national income. Eventually there was, as an important item, the replenishment of stocks.

The Three-year Plan was started with depleted stocks of raw materials, semi-finished, and finished goods. According to expert estimates the expansion of production, which the Plan provided for, would necessitate an increase in stocks to the value of 6,000 to 6,500 million forint over the whole Plan period. The planners never made any allowance for this item in their estimates of the improvement of consumption. In fact, the replenishment of stocks on the scale suggested taxed current consumption at a yearly rate of 9 to 12 per cent of the national income.

In the following table the attempt is made to estimate the proportion of the national income left for consumption.

[1] As shown in Chapter VII, out of a Plan investment totalling 6,300 million forint the amount covered by the budget was 4,300 million.

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1948	*Total Index*	*Food*	*Clothing*
January	128·4	153·1	113·2
February	132·6	159·9	113·2
March	130·0	154·8	112·7
April	130·6	156·3	112·1
May	132·5	158·5	112·8
June	124·2	142·1	112·8
July	117·0	128·0	112·8
August	115·2	124·1	113·4
September	110·1	113·9	114·0
October	114·8	120·6	114·0
November	115·7	122·8	112·6
December	115·3	122·3	112·6
1949			
January	113·9	119·6	112·6
February	111·4	114·6	112·6

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TABLE V

FINANCE AND CREDIT

(1) *Budget*

	1937–8	*1946–7*	*1947–8*	*1949*
	million forint			
Total expenditure of which	6,215	3,701	6,300	13,000
Current on goods and services	5,755	2,265	3,758	—
International commitments	—	1,436	1,709	—
Plan investment	—	—	833	4,300
Total revenue of which	6,178	3,703	6,397	—
Current	6,084	2,891	6,047	—
Borrowing and other extraordinary	99	812	359	—

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(2) *National Bank of Hungary*

	Gold and Foreign Exchange	*Bills*	*Loans on Current Account*	*Advance to Treasury*	*Notes in Circulation*	*Sight Liabilities*	*Deposits*
				million forint			
1946							
31 August	278	374	—	—	356	147	—
31 December	338	495	—	342	968	161	—
1947							
31 July	501	920	—	340	1,592	93	—
31 December	501	1,663	—	340	1,992	319	—
1948							
31 July	452	1,730	779	340	2,224	334	730
31 December	556	50	5,981	337	2,817	29	3,691
1949							
31 July*	600	3	7,331	309	3,094	3	4,716
31 December	512	—	8,557	288	2,629	3	6,492

* Banking reform in progress.

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(3) *Total Deposits of Commercial Banks and Savings Institutions*

	million forint
1938	11,630
1946 August	81
December	435
1947 July	791
December	1,265
1948 July	1,432*

* Including 389 million forint held by the National Bank, the transfer of the assets and liabilities of the other banks to the National Bank being in progress.

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TABLE VI

DEVELOPMENTS IN TRANSPORT

(1938 = 100)

Goods	*1946–7*	*1948*	*1949*
Railway	77·8	128·8	148·6
Road	183·7	218·7	223·4
Shipping	22·6	68·0	76·0
Passengers			
Railway	120·0	204·0	222·0
Road	58·0	159·0	289·0

TABLE VII

CAPITAL EXPENDITURE UNDER THE PLAN[1]

	1947–8	*Total Plan Period*
	million forint	
Agriculture	688·0	3,255
Mining and industry	792·0	2,987
Communications	545·4	1,957
Building (urban housing, social, and cultural)	468·7	1,844
Total	2,494·1	10,300*

* Inclusive of 257 million forint trade investment.

TABLE VIII

DETAILS OF INVESTMENT IN 1947–8

	Million forint	*Per cent of Programme*
Agriculture		
Directly into agricultural production	335·2	127·3
Agricultural training	24·4	97·4
Industries serving agriculture*	124·6	109·3
Rural electrification, housing, and roads	203·7	115·1
Total	688·0	118·7
Mining and Manufactures		
Mining	161·5	115·4
Iron, steel, non-ferrous metal, and engineering	293·9	124·5
Electrical power generation	143·2	286·4
Textiles	68·9	186·3
Chemicals	64·5	97·8
Miscellaneous†	59·8	196·3‡
Total	792·0	143·0
Communications		
Railways	238·9	136·0
Roads	159·4	146·8
River, air, tramway, and postal services	147·0	102·8
Total	545·4	127·6

* Including the production of tractors, fertilizers, etc.
† Including building materials, food, leather, paper, and wood manufactures.
‡ Excluding leather for which no target is given.

[1] [The Hungarian Three Year Plan of 1947-9--Analyst]

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	Million forint	Per cent of Programme
Building		
Urban housing	111·7	144·9
Hospitals and other social service buildings	117·0	143·5
Schools and scientific institutions	55·3	113·0
Administrative buildings for general and local authorities*	184·7	772·9
Total	468·7	199·2

* Including aqueducts and sewage installations.

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TABLE IX

1947–8 PRODUCTION IN MINING AND MANUFACTURES COMPARED WITH PLAN AT JANUARY 1947 PRICES

	Million Forint	Per cent of Programme
Total Mining	754·1	106·4
Steel (unmanufactured)	373·8	108·9
Total Manufactures	12,468·4	104·5
Iron, non-ferrous and engineering	3,455·7	123·3
Electricity generation	680·5	120·9
Chemicals	1,260·1	109·3
Textiles	2,319·7	95·2
Food industries	2,865·1	86·8
Other industries	1,887·2	112·5

TABLE X

1949 PRODUCTION IN MINING AND MANUFACTURES COMPARED WITH PRE-WAR

(1938 = 100)

Iron ore	114	Bicycles	283
Bauxite	104	Motor bicycles	728
Coal	127	Electric power	168
Crude oil	1,169	Cement	162
Steel	131	Sheet glass	244
Aluminium	1,110	Phosphate fertilizers	208
Machine tools	3,040	Nitrate fertilizers	182
Railway waggons	320	Vegetable oils	182
Locomotives	822	Cotton fabric	119
Lorries	190	Woollen cloth	125
Tractors	470	Footwear	122
Agricultural machines	332		

THE BILLION PENGOE PLAN OF 1938

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In March 1938, the Hungarian Government announced that legislative steps would be taken to enable the government to carry out a Five Year Plan to improve the defensive powers of the country and foster industrial and agricultural production. The motives of the plan were twofold. One was to increase and equip the army and make up for the disparity in military strength relative to Hungary's neighbors caused by the limitations on armaments imposed by the Peace Treaty of 1920. The second was to forestall a serious setback in the boom which, started in 1933, showed signs of slackening in the second half of 1937.

Total costs were estimated at 1 billion pengoes,[1] that is, 200 [454] million pengoes per year. This meant roughly doubling the volume of investments which had swallowed up rather less than 6 percent of the national income. Six hundred million pengoes [652] were to be covered by taxes. A special progressive capital levy was introduced for the purpose and was to be paid in ten half-yearly installments. Four hundred million pengoes were to come from a loan. The first part of the loan was taken over by banks, insurance companies and business corporations, and propaganda and some pressure was used to enlist popular support.

Roughly three fifths of the billion pengoes were to serve the army and industry, one fifth was assigned to transport and communications, and one fifth to agriculture. Besides the expansion of heavy industry demanded by military considerations, the principal projects listed in the act of parliament were the following:

(a) improvement of the transport and communications system through the building of roads and bridges and other installations;

(b) speeding up the execution of an ambitious irrigation scheme, begun in 1937, involving the irrigation of 172,000 hectares[2] of land and carrying out regulatory work on rivers and inland waters;

(c) encouraging the investigation and better utilization of the country's mineral wealth and raw materials in general;

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1. One pengoe (1938) - $0.19. Official rate: $0.294
2. One hectare = 2.471 acres

(d) the fostering of agricultural production and the improving of marketing organization;

(e) improving technical instruction in agriculture;

(f) resettlement of some of the landless agricultural population;

(g) improving rural housing, health, and social services.

No detailed and comprehensive plan was drawn up and no special machinery was created to coordinate and control the plans prepared by individual government departments and agencies which usually meant the extension of their routine activities and the speeding up of the execution of projects already undertaken. It was not until 1940 that the Minister of Finance became officially the coordinator of the government's economic policy and that a Supreme Economic Council was set up, an advisory body, including, besides the heads of government departments and agencies, the under-secretaries, the assistant secretaries and the leaders of special interest groups.

The lack of a detailed plan makes it difficult to evaluate the measure of achievement and success. The exigencies created by the territorial changes of 1939-1941 and the war distorted even the faint outlines of an overall plan that could at first be discerned. This, however, is not to say that the effects of the investment program could not be felt, especially as it assumed much greater proportions than was originally intended.

Due partly to the 84 percent increase in territory and the 58 percent increase in population, partly to the pressure of war time needs, and partly to rising prices, the scope of the investment program was repeatedly extended. In two and a half years, 1.65 billion pengoes were spent and a revision of the program brought the total to be invested first to 2.6 billion pengoes, and by another revision at the end of 1943, to 4.5 billion pengoes. The capital levy which was to cover 600 million out of the original 1 billion pengoes and was to be levied in five years was all collected by the end of 1940 and new taxes and loans had to be resorted to in order to provide the additional funds required. In spite of the liquidity created by an inflationary boom, in an increasing measure the Bank of Issue became responsible for financing the scheme.

The effects of government spending were felt first of all in heavy industry. A number of plants were built which considerably increased industrial capacity. Still more would have been accomplished had the war, which reached Hungarian territory in 1944, not stopped construction work and had it not brought

THE TEN YEAR PLAN OF AGRICULTURE OF 1942

The second attempt at planning was the Ten Year Plan of Agriculture. It was introduced in 1941 in the form of a bill and was put into effect in 1942. The growing pressure of the war effort interfered with its execution and it came to an untimely end in the general upheaval in 1944.

The plan was more an investment than a production plan. While it counted on an increase in output, this was not specified. As regards investments, it was not an all-out effort to provide for the most urgent capital needs of agriculture in order to attain a prescribed production and efficiency level. In fact, as in the course of the execution of the Billion Pengoe Plan of 1938, emphasis shifted in favor of manufacturing industry at the expense of agriculture. The Ten Year Plan tried to restore the balance by enabling the Ministry of Agriculture to extend its current program by increasing its budget. It also authorized financial assistance to farmers in the carrying out of improvements specified in the act.

The plan provided for investments of 100 million pengoes per year over a period of ten years, giving a total of 1 billion. The annual installments were to be provided within the framework of the budget and were to be covered by ordinary revenue. But the government was authorized to mobilize funds by means of Treasury guarantees of credits, should the budgetary means be insufficient.

To appraise the sum of 100 million pengoes per annum, it must be remembered that, as a result of the territorial changes of 1939-1941, the territory of the country was 84 percent greater, the population 58 percent greater, and, due to the character of the recovered territories, the relative importance of agriculture also increased. The increase of the national income was smaller than that of territory or population.[1] Also there had been a

1. The territorial changes brought about in the period 1939-41, which substantially affected the economy of Hungary, were the following:

November 1938, under the first Vienna Award, the southern strip of Czechoslovakia was reincorporated into Hungary—12,100 sq. km., population 1.1 million.

March-April 1939, the occupation of Ruthenia, or Podkarpatska Russ, reincorporated 12,200 sq. km., population 0.7 million.

August 1940, under the second Vienna Award, the northern part of

marked increase in prices since 1938. Reduced to the prewar territory and in 1938 pengoes, annual investments would have been of the order of 30-40 million pengoes, giving a total of 300-400 million pengoes.

The act did not provide special machinery to carry out the plan. An overhaul and reorganization of the agricultural administration was proposed, a measure which in any case was overdue, but the act did not go into details. One innovation, specifically mentioned, was the appointment of agricultural officers to all the larger villages and to groups of smaller ones to control the execution of decrees of an agricultural-technical character and to give advice on agricultural matters to the local councils and the farmers. Hitherto the organization of the agricultural administration was curiously deficient, as it had officers only in larger territorial units which were too large for efficient control.

The other innovation was the setting up of the National Council of Agriculture, an advisory body, appointed by the Minister of Agriculture. Otherwise, the role of the Chamber of Agriculture did not change and the special interest groups of farmers were to continue to exercise their functions.

The powers of the minister were greatly increased. The minister could compel producers of special lines to set up organizations to represent their interests. To regulate supply and improve distribution, the minister was also authorized to set up organizations combining producers, processers and distributors to regulate production and prices with binding force for all concerned; he was also authorized to give monopolistic rights to cooperative societies or state organizations for the purchase, distribution and export of specified agricultural products.

Increases in production were to be brought about by investments, by temporary tax rebates to farmers making permanent improvements, and by greatly increasing the power of the Minister of Agriculture to compel farmers to adopt more efficient methods.

Investments included increasing the number and improving

Transylvania was reincorporated—43,500 sq. km., population 2.6 million.

April 1941, the occupation of part of Voivodina added 11,500 sq. km., population 1.0 million.

In 1941, Hungary had a territory of 172,200 sq. km., with a population of 14.7 million, against 93,100 sq. km. and 9.3 million in the Trianon territory.

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Table VII

VOLUME OF GOODS AVAILABLE FOR CONSUMPTION
1938, 1946-47, 1947-48, 1949-50, 1950, 1954 (planned)

Billion forints at January 1947 prices

	1938	1946-47	1947-48	1949-50 (1949)	1950	1954
National Income	21.623	13.989	18.746	(26.809)	(29.600)	(43.700)
Balance of foreign trade	-1.103	.118	.440	N.A.	(-)	(-)
Total	20.520	14.107	19.186	(26.809)	(29.600)	(43.700)
Operational expenditure of public authorities	2.830	.916	1.655	(2.000)	(3.000)	(4.000)
Reparations, etc.	-	1.436	1.223	(.600)	(.600)	(-)
Investments	1.205	.530	1.987	(4.800)	(6.300)	(9.400)
Increase in livestock	.168	.182	.387	(.500)	(.500)	(.500)
Grand Total	16.317	11.033	13.934	(18.909)[a]	(19.200)	(29.800)
Increase in inventories						
Social Democratic Plan	(.726)[c]	(.8-.900)[d]	2.091	1.971	(2.000)[e]	(3.000)
Planning Office (Nagy, op. cit.)			.770[f]	.900[f] (1.500)		

Source: National Planning Office, Report on the First Year of the Three Year Plan (Hung.) and Final Report on the Three Year Plan; J. Judik, The Three Plan, Hungarian Economic Review, 1947, Nos. 1-2, p. 32, Act XXV of 1949 re the First Five Year Plan of the Hungarian People's Republic.

Note: The figures for 1949, 1950 and 1954 are estimates, based on incomplete official data.

a. A Memorandum of the Hungarian Institute for Economic Research gives 16.913 billion forints. The provisional estimate of the Planning Office was 17.170. Both estimates were made at the end of 1948 and the latter took no account of the increase in inventories.

b. The text of the Five Year Plan gives the figure as 185 percent of prewar. It also says that it will be 140 percent of 1949, which would give 23.0 billion for 1949. Presumably the first figure is expressed in January 1947 prices, the second in the new Plan prices.

c. Cf. Judik, op. cit., p. 33.

d. Hungarian Institute for Economic Research, Report on the Economic Situation, No. 54, p. 168.

e. Assuming that stocks had reached about prewar level and that, as before the war, about one third of the investments were required to increase inventories.

f. Both in comparison with prewar and with the Social Democratic Plan, the figures seem to be much too low.

12: Free Europe Committee U-4 (no date) 1954 EC1 Hungary EC1

THE OIL INDUSTRY IN THE HUNGARIAN ECONOMY

121 Any study of a given sector of the Hungarian economy must take into account the very great changes in the economic climate as well as the frequent changes in the area and political system of Hungary.

101 The Hungary of the final third of the nineteenth century, when the Hungarian oil industry first began to develop, extended over the whole Carpathian Basin and was an integral part of the Austro-Hungarian Dual Monarchy.

652 439 From 1867 to the outbreak of World War I there was virtually no government interference with internal trade or with domestic industries that faced no competition from abroad. Theoretically at least, the official policy of the Hungarian government in this period was characterized by economic liberalism. The general level of taxation was very low.

A benevolent paternalistic attitude did prevail, however, toward industries facing competition from the Austrian part of the Dual Monarchy. Subsidies, preferential treatment in the awarding of government contracts, "buy Hungarian" campaigns, and similar methods were resorted to. These measures, of course, were not in line with the official economic policy and at times eclipsed it. Nevertheless, they were largely unsuccessful, because the simplest and most effective measure, tariff protection, could not be resorted to against Austria.

Protective tariffs, however, were imposed on selected imported manufactures and commodities. Among the latter was crude oil, first bought from Russia (1885-1895), then from the United States (until 1900), and finally

THE OIL INDUSTRY IN THE HUNGARIAN ECONOMY

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from Romania (1890-1916). These imports gradually declined in importance as Austrian (Galician) and, to a lesser degree, Hungarian, crude oil production developed.

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Oil exploration until 1894 was on a small scale and was mainly of a local nature. Since no commercial deposits were discovered, from 1894 to 1907 the government granted small subsidies to encourage further exploration. In 1907 the government began to undertake its own exploration (geological surveying) and Section 6 of the Law of 1911 declared all natural hydrocarbons a state monopoly. Subsequently, numerous concessions were granted to Hungarian as well as foreign companies under this law.

Natural gas, which had found considerable industrial utilization by the end of World War I, was discovered in Transylvania in 1909.

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On the over-all economic scene World War I brought about a great upswing in industrial activities and some controls. During the artificial boom created by the war all basic industries were expanded greatly.

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The Treaty of Trianon, 1920, brought complete separation from Austria; it also brought the loss of more than two-thirds of Hungary's land area and some three-fifths of her population. The Dual Monarchy's tariff-free market of fifty million people was reduced to a market of little more than eight million. The lost territories included all the regions where oil and gas prospecting had taken place. Slovakia and Ruthenia in the north went to Czechoslovakia; Croatia, Bachka, and the Mura district in the south were incorporated into Yugoslavia; while Romania obtained Transylvania and adjacent areas in the east.

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The dislocations caused by the war, by the ensuing disturbances, and by the enormous loss of territory brought the whole Hungarian economy to the verge of chaos.

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In 1924 the government adopted a policy of high tariff protection for industry by which Hungary, like her neighbors, aimed at self-sufficiency.

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neighbors, aimed at self-sufficiency. Industry was granted additional subsidies in the form of loans, cheap factory sites, and other measures. Together with low world market prices this policy was responsible for the depressed state of Hungarian agriculture from 1928 until about 1934, but all subsequent governments adhered to the industrialization program and frequently carried it further.

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The runaway inflation of the mid-twenties disrupted the country's finances, wiping out individual savings and ruining many companies.

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During the early twenties the Hungarian Oil Syndicate (an affiliate of the Anglo-Persian Oil Company) started explorations in western Hungary while the government carried out explorations east of the Danube. However, the Hungarian Oil Syndicate lost most of its exploration funds during the period of inflation and this coupled with unsuccessful drilling operations forced the company to abandon operations and pull out of Hungary. The government was also unsuccessful in this period, its only discovery that at Bükkszék, which resulted in the production of only 92,500 barrels over a thirteen-year period, much of it at an actual financial loss.

In 1933 the government granted a five-year concession for all areas west of the Danube to Eurogasco (an affiliate of the Standard Oil Company of New Jersey) in return for a pledge that $300,000 would be spent on prospecting and that at least eight wells would be drilled. Eurogasco's activities led to the discovery of the first commercial oil field in 1937 situated at Lispe, Zala County, near the old wells of the Mura district which were ceded to Yugoslavia in 1920. In 1940 a second field was developed nearby, at Lovászi. An eight-inch pipeline connecting the Zala fields with Budapest was completed in 1941. In that year Hungary reached self-sufficiency in oil production, and her 1943 output of 838,000 tons of crude contrasted with a (controlled) civilian consumption of only about 321,000 tons of refinery products (about 380,000 tons of crude equivalent). Table VI gives the civilian consumption for the years 1940-1943. More than half of the pro-

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[Cf. page 88, category 116--Analyst]

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473 duction was thus available for the armed forces or for export to Germany.

A new operating company, the Hungarian-American Oil Company (MAORT), a subsidiary of Eurogasco, obtained a forty-year concession soon after the Lispe discovery under the same arrangements as had been made with Eurogasco whereby the royalties to be paid to the government were fixed at 15 percent of the crude oil and 12 percent of the marketed natural gas production. MAORT achieved such successful results that in less than six years it became Hungary's third largest industrial enterprise and, considering the indirect effects, probably the largest single corporate contributor to the national income.

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439 During the late thirties the economic aspects of agri-
652 culture improved due to ever increasing agricultural exports to Germany under the Hungarian-German trade agreements, even though protection of industry remained the official policy of the government.

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131 In 1938 Hungary began to rearm. With Axis support parts of the territories lost in 1920 were recovered from Czechoslovakia in 1938 and 1939, from Romania in 1940, and from Yugoslavia in 1941. As a result, the country's area increased from 93,073 square kilometers in 1938 to 170,869 square kilometers in 1941 with a corresponding increase in population from less than 9 million to 14.6 million. In 1941 Hungary entered World War II on the German side.

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464 Rearmament, the recovery of about half of the pre-
241 Trianon territory, and finally war gave a tremendous impetus to the economy. Industrial employment rose from 289,000 in 1938 to 392,000 in 1943 (excluding the recovered areas), and, for the first time, the value of the industrial output surpassed the value of agricultural production.

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434 Government controls gradually increased. The
185 allocation of raw materials and the rationing of food and gasoline were introduced, and for the first time in Hungarian history the government embarked on large-scale economic planning.

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The "Billion Pengő Plan," officially known as the Five-Year Plan of 1938, was primarily a result of military considerations. Originally calling for an investment of one billion pengős, it was repeatedly revised upward until it reached 4.5 billion by 1943. Roughly three-fifths of the total funds were devoted to rearmament and to the heavy industries, while transportation and agriculture received one-fifth each. The plan was financed by a progressive capital levy and by government borrowing. It was carried out through the existing ministries by simply expanding their activities. A Ten-Year Plan for Agriculture calling for the investment of 100 million pengős annually was launched in 1942, but wartime dislocations prevented its realization.

By the spring of 1944 the power, aluminum, chemical, and oil industries had been considerably enlarged. The total Hungarian refining capacity was estimated as 3.5 million barrels annually before the territorial losses of 1920; as 1.5 million barrels in 1920; and was 3.2 million barrels in 1940. In contrast to this relatively modest development, by the spring of 1944, the total capacity had increased to more than 10 million barrels, only 710,000 of which were from refineries located in the temporarily recovered areas. The new plants at Pét and Szőny, which were built by the government within the framework of the Five-Year Plan of 1938, had a combined capacity of 3.6 million barrels; these plants alone considerably exceeded the total 1940 capacity.

During World War II numerous concessions were granted to German and Italian as well as domestic oil companies in the areas east of the Danube and in the recovered areas. These groups carried out extensive geophysical surveying and a few test wells were drilled. However, it was only in the Mura district, close to the Hungarian Zala fields that commercial discoveries were made. Small-scale production began in 1943. Two years later, in 1945, Yugoslavia recovered the district once more.

At the end of World War II the economy was once more at a standstill. In 1945 agricultural production did not reach one half of prewar production, while industrial output was only a fraction of that of 1938. Of 4,341 factories

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was at once a reconstruction, production, and investment program, with emphasis on the first, those investments that would have an immediate effect on production and would eliminate bottlenecks being given priority.

A National Planning Office was set up to detail the plan, which had been approved only in outline by the party leadership. The Investment Bank and the Bank of Issue were in charge of financing operations. All activities were supervised by the Supreme Economic Council and by the Cabinet.

Of the investment of 6.6 billion forints called for by the plan (1 forint was equal[1] 8.52 United States cents at the official rate), agriculture was to receive 2.0; mining and manufacturing, 1.7; transport, 1.7; and building, 1.2 billion forints. Included under "agriculture" were such items as tractor and fertilizer plants, road building, rural electrification, irrigation projects, and the establishment of tractor stations. Sixty-seven percent of the total was to be met from treasury funds (taxes and loans), 18 percent by local authorities and government agencies, and the balance by cooperatives (4 percent), remaining private sources (9 percent), and Soviet-Hungarian companies (2 percent).

After a very promising start the plan was speeded up and it was concluded by 1 January 1950 instead of 1 August of the same year.

Oil was among the few basic commodities that fell considerably short of the goals. The plan called for production of 540,000 tons in 1947/48 and for 660,000 tons in 1949/50 which was later moved up to 1949 under the speed-up program. In contrast with these high expectations the actual output was only 475,000 tons (3,600,000 barrels) in 1948 and a little below 500,000 tons (3,800,000 barrels) in 1949. Thus, only 75 percent of the plan was fulfilled in oil production, and the 1949 output remained at but 59 percent of the wartime peak of 1943.

While mechanization in agriculture progressed, 211

[1] [sic -- Analyst]

161 This trend ? was aggravated by the fact
458 that Hungary was such a densely populated state. The
241 density of her population amounted to almost 100 people per square kilometre. Due to the low agricultural prices prevailing generally in the world, to the keen foreign competition and to her dependence upon the exportation of raw products it was almost impossible adequately to maintain the agrarian population by the cultivation of the soil.

728 While her old Austro-Hungarian market of 58 million
439 people was reduced to a market of 7·5 million, she was
652 burdened in addition with large foreign debts which could only be paid by agricultural exports. Owing to political considerations, the surrounding countries, instead of absorbing the Hungarian surplus products, boycotted her during the early post-war years. Added to this, the economic and other restrictions of the peace treaty made it impossible for Hungary to pursue an independent economic policy serving the true needs of the country. Not until eight years after the end of the first world war was the Government able to introduce an economic policy (industrialization, protective tariff system etc.) which could meet the challenge of the density of population and prevailing unemployment.

728 The difficulties of the post-war years were aggravated
464 by the existence within her borders of hundreds of thousands of refugees from former Hungarian territory. Our educated classes had grown numerically so great that it was practically impossible to find places for everyone in
652 the administration and economic systems. Millions had
185 to be spent on measures serving solely charitable purposes out of the proceeds of production and out of greatly decreased state receipts, which fell off as a result of the effects of the war. Therefore, for the first few years, no

? [i.e., a reversion to more primitive conditions -- Analyst]

planned social policy of bolder conception and projecting into the future could be instituted.

Social progress was obstructed also by other difficulties. The Government of Hungary consistently endeavoured to raise the living standards of the people. Several circumstances, beyond the control of political leadership, occasionally thwarted such efforts. When the period marked by the aforementioned economic boycott came to an end, several waves of depression swept over Europe, and by these Hungary was always seriously affected.

The liquidation of the post-war inflation was done under the financial supervision of the League of Nations, which meant that we did not enjoy full financial sovereignty. The same thing took place a second time after 1931 when the Central European economic and financial credit crisis occasioned new control. In spite of the exceptionally adverse conditions Hungary did not halt on her way to social advancement, but from the beginning the interests of social welfare constituted the key-note of her efforts to harmonize her economic and political life. In the enactment of all laws in the economic and financial sphere, social problems were given foremost consideration at all times during the past twenty years.

The march of social advancement was retarded at intervals by the world-wide depression, and therefore social conditions in Hungary could not progress all along the line as rapidly as was desired by the Government. Nevertheless the achievements have been great. In several respects, as we shall see, the social reforms were far in advance of those undertaken by larger and more wealthy nations, while again they can be considered as trail-blazers in some of their implications.

2/7 [cf., category 116, p.8 -- Analyst]

with certain permanent social welfare purposes (public charity, documents for paupers, physical training etc.).

Social credit grants.

The vast credit schemes launched by the Government were mostly of social significance. The most extensive debt adjustment in Hungary since the first world war was aimed at the promotion of the social welfare of the agrarian population, which was gravely affected by the world-wide agricultural slump. The indebtedness of farmers and the fall of prices was so great that it was beyond the Government's ability to remedy the situation according to established financial and economic policies. In the beginning the Government came to the aid of the farmers by lowering the interest rates and prohibiting public sales of real estate. Later the policy of protected ownership was instituted, and the Government extended the amortization of farm debts over a longer period.

Part of the short term bank loans contracted by smaller farmers were paid by the Government. Indebted farmers owning less than 70 acres of land were especially favoured by the adjustment of their debts. The social implications of the protected ownership system will be discussed in the chapter dealing with agriculture.

Interest rate reduction.

When lowering the interest rates on farm debts the prime consideration was that the burden of the poor should be lighter than that of the rich. We mention here that the general lowering of interest rates benefited the whole community, and further, that the interest rates on small loans contracted with state pawnshops were reduced to a third.

[cf. category 116, pp. 39-51 -- Analyst]

Loans to small industries and to shopkeepers.

652 452 The following Government activity in the credit field assisted the social and economic strengthening of certain classes: 30 million pengős have been loaned to small industries up to date. Artisans not able to provide security required by the banks received loans from the Government of 300 to 500 pengős at a very low rate of interest. To aid the reorientation of commercial life the Government is extending credits up to 30 million pengős to shopkeepers. A specially reduced rate of interest is charged to shopkeepers with large families.

Other social welfare credit activities.

To alleviate unemployment among the educated classes and to ensure the replenishment of their ranks, financial assistance was given to deserving educated men in order to set them up in gainful occupations. Here is a brief summary of other public credit schemes: Loans granted to civil servants totalling almost 30 million pengős up to date; advance interest payments to holders of war bonds amounting to 60 million pengős; credits granted to the banks of the reoccupied territories in order to stabilize their finances; credits to relieve the difficult financial position of the insurance companies; and financing the different social welfare activities instituted since the war to provide food and clothing for the needy.

Housing Projects.

652 362 452 Public credit policy evidenced noteworthy results in helping to solve the housing problem. Some of the housing

projects are nearing completion, others are still being formulated. The most important are the following:

LAB. Loans.

Act XLI of 1930 made it possible for civil servants and small investors to contract long term building loans on advantageous terms. During the last 11 years 45, 300,000 pengős have been advanced for this purpose, and out of this amount 6000 family homes and more than 80 large apartment blocks were built. The project was financed by the issue of Government bonds. These were taken up by the banks and social insurance companies.

Building in villages.

More than a quarter of a million building lots were allocated among the villagers during the first land reform. In 1927 the Co-operative Rural Building Society was established by law. This society loaned more than 60 million pengős for the erection of approximately 43,000 family homes in villages up to 1940.

Building activities of the OTI.

The largest social insurance company in the country invests its old age and disability reserve funds in building loans. Among the results of its widespread activities in this field, the following may be mentioned: at Albertfalva a garden city was built, in the XIIIth district of Budapest 752 family homes were built for workers, and another garden city was built at Pócsmegyer, several large apartment houses being erected by the society, housing thousands of people.

Building activities of the MABI.

The Insurance Board of Business Employees plays an important part in housing projects. Its investments in housing amount to 17 or 18 million pengős.

Capital City of Budapest.

The Capital City of Budapest borrowed 20 million pengős from social insurance companies to build 3000 small homes, half of which are already completed.

National Folk and Family Protection Institute.

This family protection project, the largest undertaken by the Hungarian Government, built 5000 homes in the first and 6000 in the second year it was functioning. The details of this organization will be given later.[1]

Industrial Retirement Boards.

The more important industrial retirement boards have invested 100 million pengős up to date in buying and building houses, and in loaning money on mortgages.

Besides carrying out long-term plans, the public policy was flexible enough to meet any unforeseen contingency. We have already dealt with the problems of post-war unemployment, and with the social and economic problems of the educated classes. In conclusion we shall relate how the public welfare policy coped with emergencies, some of which were disasters due to the elements, and some the result of exceptional times. Most of these problems had to be solved promptly by the state and society working together.

[1] [cf. category 116, pp. 46-47 --- Analyst]

653 military service, and consequently the income of the seasonal
729 workers was negligible. The solution was reached by the Government in combining the employment of returned soldiers with the performance of public works such as rebuilding the homes of flood victims, and defence projects. Public works costing 54 million pengõs bridged over the last months of the depression until the period of accelerated war-time production.

Providing for the refugees.

729 The refugee problem was an important item in the
167 Hungarian social welfare administration. Hungarian
659 resources were strained to the utmost in providing for the periodic influx of refugees from the former Hungarian territories. Immediately following the first world war this flow was at its peak, as we have previously stated. A similar situation occurred a second time when part of Transylvania was reoccupied. Hungarians who were left under foreign domination started to move across the new boundaries in large numbers. In order to help them to become self-supporting and be readily absorbed into economic life the Government settled them in various parts of the country. During this period of rehabilitation, from the autumn of 1939 till the end of 1942, the state spent 25 million pengõs on their maintenance.

Compensation of war bond holders.

652 During the last twenty years it was often necessary
454 from the standpoint of social security to protect the interests of the small investor. In the first world war thousands had put all their savings into war bonds, and when these lost their value many of the bondholders were in dire straits. For

a long time the state was not in a position financially to restore even fractionally the original value of the war bonds, but the bondholders of limited means received Government assistance. State expenditure under this heading has amounted to 60 million pengős since 1928. The war bonds were revalued in 1942 by Act of Parliament. The bonds are now worth 5% of their original value except those of small denominations, which can be cashed at 10% of their original value. Those who were entitled to Government assistance from their war bonds will continue to receive such grants-in-aid.

Protection of the small investor.

The interests of the small investor required governmental aid at other times. The Hungarian banking institutions survived the many economic depressions (with the exception of the post-war inflation) without serious disturbance to their financial structure and without inflicting a loss on their depositors. After the consolidation of public finances it seldom became necessary for the Government to intervene on behalf of the depositors, except in the case of banks in the re-occupied territories. The Government had to render financial assistance to these to tide them over the period of re-organization. Only when the Phönix Insurance Company collapsed was there some danger of many small investors suffering losses, but steps taken by the Government averted the danger and put the whole insurance system on a sounder basis.

Social Housing Projects.

The problem of adequate housing for the industrial population in urban districts became acute during the

425 sional reform, but only by carrying out a continuous and
241 progressive programme.

The System of Protected Ownership.

241 The greatest blemish on the economic and social
426 structure of the agrarian community was the heavy in-
458 debtedness of the farmers. During the prosperous years after 1927 with their favourable prices and ready market, the farmers contracted extensive debts for making capital improvements in their land. The precipitous drop in farm income due to the financial crisis of 1931 left some of the farmers unable even to meet the interest payments on their debts. Wholesale foreclosures threatened, and the world-wide depression barred any hope of tens of thousands of farmers remaining secure in their tenure without outside help.
241 The Government, fully cognizant of the danger threatening
426 them, came to their rescue by first reducing the interest rate
652 on farm debts and then by prohibiting foreclosures. When these measures were found to be insufficient, the Government created the system of 'protected ownership' Under this system the interest payment relief and prohibition of foreclosures were continued and the Government also made provision for the definitive settlement of farm debts.

The small farmers were the ones who reaped the greatest benefits from this system. Among other grants-in-aid the Government paid gratuitously part of the short term bank debts of those farmers who cultivated less than 20 Hungarian acres of "protected" land. This was done before the general settlement of the farm debts took place, which covered these farmers also. During this settlement the Government assumed as a book debt that part of the farmers' indebtedness which was in

excess of their registered yearly income multiplied by forty. The owners of farms of less than thirty Hungarian acres received further aid by having their short term indebtedness under the above limit converted into long term debts repayable in ten years by annual instalments which did not exceed 4·5% of the outstanding amount. Another regulation favoured the owners of less than fifty acres of land by releasing them from any joint obligation which they undertook in the interest of a third party. The protected ownership system proved so successful that the financial position of the protected owners became strong enough to enable them to repay their debts in part or in some cases in full. When the debtor made payments on the capital borrowed, the Government awarded him an amortization grant. The amount of this grant was 10% —15% of the capital repaid by the larger estates and 20% by farmers owning less than ten acres.

The legal measures regarding protected ownership substantiated in every respect the social ideals upholding the interests of the small farmer. In order to verify this statement we give the following figures:

In Hungary the majority of the 78,000 farms covered by the protected ownership system were farms of less than twenty Hungarian acres. The number of the latter reached almost 69,000 and were owned by almost 120,000 people. If we take their families into consideration it means that over half a million people benefited by the system. To sum up: the protected ownership system saved from ruin the means of livelihood of half a million people, because if the Government had not come to their aid this multitude would have been added to the numbers of the landless.

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selected from all major labor unions is headed by an ardent Communist, Kossa, organizer of the Budapest streetcar workers union.

An essential institution in Hungarian industry is the factory committee, elected by the workers to represent their interests in dealing with the management, or with State officials now serving as replacements for an almost extinct managerial class. These small factory committees are particularly sensitive to party ideology and are permeated by Communist propaganda. Through them the workers are brought into constant contact with political authorities of the State, and their private life is closely watched. At their trade union meetings they are given lectures on foreign and domestic politics devoted frequently to violent hate propaganda against Britain and the United States.[43] Trade unions and factory committees have thus become important tools in the hands of the country's dominant political-economic bloc.

The process of industrial recovery and the strengthening of a new laboring class have suffered considerably by the recent financial disaster which culminated in the inflation of 1946. The country's economic foundations were first weakened by the wave of German looting and seizures of valuable assets and capital goods, estimated at approximately ten billion dollars. The economic deathblow was then delivered by the prompt acquisitiveness with which Soviet Russia reduced occupied Hungary to the role of an economic colony. The threatening upward spiral of prices, wages and nominal money values finally drove out the Pengö, discredited by a long and unchecked period of inflation. The economic situation improved substantially after the stabilization of August 1946 when an old Austro-Hungarian monetary unit, the *forint* (florin), had been established as the fixed national currency. By the end of 1946 industrial capacity was gradually restored to about sixty percent of the pre-war potential, although Hungary continued to pay an exceedingly heavy reparation bill, both in industrial equipment and in current manufacturing production.[44]

Reparations today include nearly all of the country's capital goods

43 Cf. "Workers and Industry, Danubian Outlook," *The Economist*, Jan. 25, 1947, p. 134.

44 N. Káldor estimates that at least one-fourth of the total current production goes to the U.S.S.R. The reparations burden is further enhanced by a strict interpretation of the Potsdam agreement according to which the Russians continue to compute the reparations bill in "dollars of 1938 purchasing power." Nevertheless, Professor Káldor reaches the strange conclusion that "the picture of Soviet Russia as the ruthless economic exploiter of Hungary is far too one-sided." Cf. "The Danubian States," *The Times*, London, Nov. 19, 1946.